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In the Supreme Court of the United States

OCTOBER TERM, 1979

FEDERAL ENERGY REGULATORY COMMISSION,
PETITIONER

v.

PANHANDLE EASTERN PIPE LINE COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

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PANHANDLE EASTERN PIPE LINE COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

The Solicitor General, on behalf of the Federal Energy Regulatory Commission,[1] petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case.

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[1] Under Section 402(a)(1)(C), (D), (E), and (F) of the Department of Energy Organization Act, Pub. L. No. 95-91, 91 Stat. 583, 42 U.S.C. (Supp. II) 7172(a)(1)(C), (D), (E), and (F), this agency has succeeded to the relevant functions and responsibilities of the former Federal Power Commission with respect to the certification and regulation of sales of gas in interstate commerce under the Natural Gas Act, 15 U.S.C. (and Supp. II) 717-717w. The term "Commission" herein refers to the Federal Power Commission or the Federal Energy Regulatory Commission, as the context indicates.

OPINIONS BELOW

The opinion of the court of appeals (App. A, *infra*, 1a-79a) is reported at 613 F.2d 1120. The orders of the Commission (Apps. C and D, *infra*, 83a-103a, 104a-108a) are not yet reported.

JURISDICTION

The judgment of the court of appeals was entered on December 20, 1979 (App. B, *infra*, 80a-82a). On March 12, 1980, the Chief Justice extended the time for filing a petition for a writ of certiorari to and including April 18, 1980, and on April 9, 1980, he further extended the time for filing a petition to and including May 18, 1980. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

QUESTIONS PRESENTED

1. Whether the Federal Energy Regulatory Commission may condition authorization to a natural gas pipeline company to perform a new transportation service using excess pipeline capacity, on the pipeline crediting the net revenues realized from the new transportation service to its regular sales customers, who, under the pipeline's existing rate structure, are paying for the excess pipeline capacity.

2. Whether such conditioning authority may be exercised only if the Commission also allows the pipeline automatically to impose on its regular sales

customers the costs of obtaining transportation services on their behalf from other pipelines in unrelated transactions.

STATUTE INVOLVED

Sections 4, 5, 7(c), and 7(e) of the Natural Gas Act, 15 U.S.C. (and Supp. II) 717c, 717d, 717f(c) and 717f(e), are set forth in Appendix G, *infra*, 126a-132a.

STATEMENT

The decision below deals with three discrete cases (consolidated for review by the court of appeals) involving Panhandle Eastern Pipe Line Company ("Panhandle"). The Commission petitions for certiorari in only one of these cases—C.A. No. 78-1356—which involves the nature and scope of the Commission's authority to condition certificates of public convenience and necessity under Section 7(e) of the Natural Gas Act. Specifically, this case concerns the Commission's power to require, as a condition of issuing a certificate, that Panhandle pass along to its regular sales customers (in the form of account credits) the net revenues it receives for a new transportation service—*i.e.*, one which it does not perform for its regular customers. The majority below affirmed the Commission's order in the second case (C.A. No. 78-1960), rejecting Panhandle's request that the costs it incurs in compensating other pipelines for transporting new gas supplies be passed along automatically

to its regular sales customers. Panhandle has not sought review of that judgment in this Court.[2]

A. The Statutory Framework

Section 7(c) of the Natural Gas Act requires all "natural gas companies" (a term which encompasses interstate natural gas pipelines) to obtain a "certificate of public convenience and necessity" from the Commission before offering new sales and transportation services subject to the jurisdiction of the Commission under the Natural Gas Act. 15 U.S.C. (Supp. II) 717f(c). The Commission, under Section 7(e), is empowered to attach to any certificate it issues "such reasonable terms and conditions as the public convenience and necessity may require." 15 U.S.C. (Supp. II) 717f(e).[3]

Section 4(a) of the Act declares that all rates charged by companies subject to the Commission's jurisdiction "shall be just and reasonable." 15 U.S.C. 717c(a). Once initial rates have been authorized under Section 7, a natural gas company may file a rate increase under Section 4; the Commission may suspend the new rates for up to five months, after which the increased rates may be collected, subject

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[2] Nor do we seek review in the third case (C.A. No. 78-1630), which involved the use of Panhandle as a billing conduit in a third transportation agreement.

[3] For example, in the exercise of this power the Commission may condition a certificate upon a rate lower than the contract rate. See *Atlantic Refining Co.* v. *Public Service Comm'n of N.Y.*, 360 U.S. 378 (1959).

to refund (with interest) of that portion of the increased rates which the Commission finds is not justified. 15 U.S.C. 717c(e).

Section 5(a) of the Act, 15 U.S.C. 717d(a), provides that whenever the Commission, after a hearing, shall find that any rate is "unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate * * * and shall fix the same by order * * *." Section 5(a) rate adjustments are prospective only.

B. The Relevant Commission Orders

1. *The Revenue Crediting Order (C.A. No. 78-1356)*

In this proceeding, Panhandle sought Commission authorization under Section 7(c) of the Act to transport natural gas for an industrial end-user (Libby-Owens-Ford Company) for an eight-year term. Because it had excess capacity for which its regular customers were already paying, Panhandle was able to provide this transportation service without incurring substantial additional costs.

The Commission authorized the arrangement, subject to a number of terms and conditions which it imposed under Section 7(e) (App. C, *infra*, 83a-103a). Consistent with its previously articulated policy,[4] the Commission reduced the term of service

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[4] See FPC Order No. 533, 54 F.P.C. 821, order on reconsideration, 54 F.P.C. 2058 (1975), aff'd, *American Public Gas Ass'n* v. *FERC*, 587 F.2d 1089 (D.C. Cir. 1978). Order No. 533 was a statement of policy with repsect to the transportation by jurisdictional interstate pipelines of natural gas sold

to two years (*id.* at 99a). In addition, because the transaction was not anticipated at the time Panhandle's rates were set in the previous Section 4 proceeding, the Commission, as a condition to the certificate, required Panhandle to credit the revenues from the new transportation service to its regular sales customers by applying these revenues to the pipeline's unrecovered purchased gas cost adjustment account (App. C, *infra*, 102a).[5]

The Commission explained on rehearing that this decision was based on its determination that the regular customers, who, under the existing rate structure, were paying for the excess pipeline capacity that enabled Panhandle to offer the new transportation service, should receive the revenues resulting from such a service (App. D, *infra*, 105a-106a). On rehearing, the Commission also amended its order to permit Panhandle to recover its "out-of-pocket costs" incurred in performing the certificated transportation service (*id.* at 106a-107a, 108a).

2. *The Cost Tracking Order (C.A. No. 78-1960)*

In this case, Panhandle's affiliate, Trunkline Gas Company ("Trunkline"), applied for a certificate of

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by certain producers from the onshore domain and the offshore non-federal domain to non-resale industrial and commercial customers for high-priority uses.

[5] The purchased gas cost adjustment clause is a mechanism that allows natural gas companies to adjust their rates twice a year through an abbreviated Section 4 rate filing reflecting fluctuations in the cost of gas, without having to file a general Section 4 rate filing showing all costs and all revenues. See 18 C.F.R. 154.38(d)(4). (See notes 8 and 14, *infra*).

public convenience and necessity authorizing it to transport, for a period of ten years, new supplies of natural gas for sale by Panhandle to its regular customers. Panhandle petitioned to intervene in Trunkline's Section 7 proceeding and requested the Commission to condition Trunkline's certificate to permit Panhandle to "track" (automatically pass through to its regular customers without a full Section 4 proceeding) the costs arising from this transportation service.

The Commission rejected Panhandle's argument that, since the Commission previously had required it in one transaction (C.A. No. 78-1356) to credit new transportation revenues to its regular customers, the Commission should permit it, in an entirely separate transaction, to track the costs it incurred in obtaining transportation for additional gas supplies (App. E, *infra*, 113a-116a). Instead, the Commission relied on the conventional principle that a pipeline should recover its additional costs by a rate filing under Section 4 of the Act, not by a direct pass-through imposed as a "condition" to a Section 7 certificate issued to another pipeline (App. E, *infra*, 114a). The Commission stated that the sale by Panhandle of additional gas supplies transported for it by Trunkline could result in the recovery by Panhandle of fixed costs over and above those allocated to the pipeline's regular customers' rates (*id.* at 116a). As a result, Panhandle's overall revenues might match or exceed its overall cost of service, even without tracking; if that turned out not to be the case, the Commission observed, Panhandle could file a

general rate increase under Section 4, where all costs and all revenues could be matched (App. E, *infra*, 115a-116a).[6]

C. The Opinions Below

On Panhandle's petition for review, the court of appeals set aside the Commission's revenue crediting requirement (C.A. No. 78-1356) and remanded that case to the Commission for further proceedings (App. A, *infra*, 16a-45a). The court affirmed the Commission's refusal to permit Panhandle to recover its new transportation costs through a tracking mechanism imposed as a condition to the Section 7 certificate issued to Trunkline (C.A. No. 78-1960) (App. A, *infra*, 45a-49a). Chief Judge Wright concurred in the result in the revenue crediting case, but dissented in the cost tracking case (*id.* at 52a-79a).

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[6] Fourteen days after the Commission's order denying Panhandle's request for a transportation cost tracker in Trunkline's Section 7 certificate proceeding, Panhandle filed a Section 4 rate increase, which became effective November 1, 1978 (Docket No. RP78-62). This rate filing reflected the new transportation costs that Panhandle was incurring in C.A. No. 78-1960. The rate proceeding was eventually settled. Under the settlement agreement, Panhandle received a transportation cost tracker, but was required to refund to its existing customers the fixed cost component of its unanticipated sales volumes as well as revenues generated from transportation services not accounted for in the rate case. Since the settlement agreement was made effective as of November 1, 1978, and Panhandle incurred new transportation costs in C.A. No. 78-1960 no earlier than April 17, 1978 (the date the Commission authorized the transaction), Panhandle lacked a transportation cost tracker for this transaction for no more than 6½ months.

1. Proceeding from the premise that the revenue crediting condition "adjust[ed] rates previously approved by the Commission for customers not receiving the services to be certificated" (App. A, *infra*, 25a; footnote omitted), the majority overturned the Commission's order imposing that condition. According to the majority, such a use of the Commission's Section 7(e) power "would emasculate the role of section 5, dilute the protections provided in sections 4 and 5 against regulatory lag and rate instability, and eliminate section 5 protections of hearing and specific findings as to justness and reasonableness of rates prior to a rate reduction order * * *" (App. A, *infra*, 31a).

"Assuming arguendo that the Commission's order was authorized by section 7" (App. A, *infra*, 42a), the majority found a second basis for setting it aside.[7] The majority held that the revenue crediting provision was in any event "unreasonable" because it did not allow new transportation revenues to be offset by the increased costs incurred by Panhandle in com-

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[7] The majority also found two other bases for overturning the Commission's revenue crediting requirement. First, it ruled that, "[e]ven assuming the revenue crediting provision * * * was within the ambit of the section 7(e) conditioning power," use of that mechanism in this case "was not supported by soundly based findings in the record * * *" (App. A, *infra*, 39a-41a). We challenge that ruling. See note 10, *infra*.

Additionally, the majority ruled that the revenue crediting mechanism violated the Commission's regulations by employing an incorrect account (App. A, *infra*, 34a-38a). While we believe this ruling to be erroneous, we do not seek its review, since the Commission can create a new account for the crediting of transportation revenues.

pensating other pipelines such as Trunkline for transporting its gas (*id.* at 44a). The majority reasoned that "such a netting procedure would be essential where both transportation costs and revenues were unanticipated—even assuming the pipeline was in other respects recovering its costs. The unforeseen income may increase a pipeline's revenues above the just and reasonable level, but the unforeseen costs, at the same time, would directly reduce the size of this 'overcollection' " (*ibid.*).

2. Chief Judge Wright concurred in part and dissented in part (App. A, *infra*, 52a-79a). In his view, the majority had "mischaracterized" the Commission's revenue crediting order by treating it "as if it were one 'adjusting previously approved rates for services not before the Commission in the relevant certificate proceeding' " (*id.* at 66a-67a). Judge Wright observed (*id.* at 67a; emphasis in original):

> *Rates* are not adjusted; only the size of future rate changes via the purchased gas account is affected. The Commission has not reevaluated Panhandle's cost of service, nor has it, as the majority implies, used the Section 7 conditioning power as a vehicle for lowering Panhandle's otherwise applicable rate of return. *All* that the first order accomplishes is to require Panhandle to dispose of *new* revenues in a particular way —*i.e.*, to flow those revenues through to its resale customers. Admittedly, those customers are better off than before the order. Panhandle, however, is *neither better off nor worse off* than before. The effect of the order is to leave Pan-

handle's rate of return at exactly the same level as before the order.

Judge Wright believed (App. A, *infra*, 70a) that the Commission has ample authority under Section 7 "to ensure that certification of a new service—such as transportation—does not create an imbalance in the pipeline company's overall profit structure." He therefore determined that the Commission properly employed its conditioning power in the revenue crediting case to "maintain the *status quo*—until a full cost-of-service proceeding is completed" (App. A, *infra*, 67a; footnote omitted). Judge Wright concluded, however, that he could not vote to affirm the Commission's disposition of the revenue credit issue, because in his view the Commission had failed adequately to explain "why it treats revenues differently from parallel costs" (*id.* at 74a).

REASONS FOR GRANTING THE PETITION

This case presents an important question concerning the Commission's ability to continue to exercise its regulatory responsibilities effectively in the face of changing conditions in the natural gas industry. As both the majority (App. A, *infra*, 3a) and Chief Judge Wright (*id.* at 57a-60a) recognized, the revenue crediting order at issue here reflects the Commission's attempt to respond to these changes.

As a result of shortages in natural gas reserves that developed in the early 1970's, many pipelines

have had to obtain gas from new sources that are often not connected to their systems. It thus has become increasingly common for one pipeline to transport gas for another company. Also, certain industrial customers have been allowed to buy gas directly from producers and to pay a pipeline to transport the gas. These sorts of arrangements entail little additional cost to the transporting company because the gas shortage has left the pipelines with substantial excess capacity that is already being paid for by the pipelines' regular customers. As a result of new arrangements of this type, pipelines have experienced substantial fluctuations in costs and revenues that were not anticipated when the pipelines' rates were set. This case involves an attempt by the Commission, in light of changing conditions in the natural gas industry, to adopt flexible procedures in order to fulfill its statutory mandate of assuring "an adequate and reliable supply of gas at reasonable prices." *California* v. *Southland Royalty Co.*, 436 U.S. 519, 523 (1978).[8]

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[8] Another recent feature of the gas industry has been a pattern of rapid increases in the cost of purchased gas. In response to rising gas costs, the Commission promulgated a regulation (18 C.F.R. 154.38(d)(4)) that permits inclusion of a purchased gas cost adjustment (PGA) provision in a pipeline company's tariffs. See FPC Order No. 452, 47 F.P.C. 1049, modified, 47 F.P.C. 1510 (1972) and 49 F.P.C. 84 (1973). This provision allows a pipeline to pass along to its customers increases in the cost of purchased natural gas without having to file frequent full Section 4 rate increases. As Judge Wright observed (App. A, *infra*, 58a-59a), the pur-

1. Under the Natural Gas Act, the Commission sets rates for interstate transportation and sales of natural gas by interstate pipelines. See generally *Consolidated Gas Supply Corp.* v. *FPC*, 520 F.2d 1176, 1179-1180 (D.C. Cir. 1975). A pipeline's total cost of service is divided between fixed costs, which remain constant regardless of changes in the level of sales and transportation volumes, and variable costs, which change with the level of those volumes. Under the rate design methodology employed by most pipelines, including Panhandle, most of the fixed costs that relate to the pipeline's capacity to transport gas are allocated to individual customers on the basis of annual volumes estimated to be sold. See *United Gas Pipe Line Co.*, 50 F.P.C. 1348 (1973), rehearing denied, 51 F.P.C. 1014 (1974), aff'd *sub nom. Consolidated Gas Supply Corp.* v. *FPC*, *supra*. A transportation rate, which is the charge exacted by a pipeline to transport another company's gas, generally reflects the pipeline's average cost of transporting the gas.

If, during the period a rate is in effect, actual sales and transportation volumes exceed those projected in the previous rate proceeding, the pipeline may recover more than 100% of its fixed costs. In order to prevent overrecovery of fixed costs derived from unan-

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chased gas cost adjustment provision—like the revenue crediting order at issue here—is an attempt by the Commission to make necessary adaptations in the statutory procedures in order to alleviate some of the problems arising from the gas shortage.

ticipated transportation services, the Commission has required pipelines—including Panhandle in this case —to credit to their regular sales customers the resulting net additional revenues. If, on the other hand, actual sales and transportation volumes are less than the projected volumes, the pipeline may be able to recover only a part of its fixed costs. In that event, the pipeline may exercise its right under Section 4 of the Act to file increased rates.

The central issue in this case is whether the Commission may exercise its broad statutory authority under Section 7(e) to condition certificates "as the public convenience and necessity may require." See *Atlantic Refining Co.* v. *Public Service Comm'n of N.Y.*, 360 U.S. 378, 388 (1959). The court of appeals significantly narrowed that conditioning power by holding that the Commission could not use it to pass along transportation revenues to a pipeline's regular sales customers where the pipeline had obtained the revenues through a use of excess pipeline capacity already allocated to the regular customers' rates. We submit that this decision is incorrect and carries the real potential of inhibiting prompt Commission action to meet the evolving needs of the natural gas industry.

The central premise underlying the majority's ruling is that, by conditioning the certificate with a revenue crediting requirement, "*the Commission has not acted just to hold the line on certificated rates, but to adjust other, previously approved rates as well*" (App. A, *infra*, 29a; emphasis in original;

footnote omitted). As Judge Wright correctly recognized, however, the Commission's order did not adjust previously established rates; rather, it required Panhandle to credit its regular resale customers with new transportation revenues to which Panhandle was not entitled. As Judge Wright stated, "[t]he effect of the order is to leave Panhandle's rate of return at exactly the same level as before the order" (App. A, *infra*, 67a).

The majority below also suggested that the Commission may have other means at its disposal to implement revenue crediting. For example, the majority noted that the Commission might approve "some sort of 'tracker' system for transportation revenues and costs" in individual Section 4 proceedings, "or it might by rulemaking adopt a policy allowing inclusion of such ["tracker"] clauses in rate filings under § 4" of the Natural Gas Act (App. A, *infra*, 32a & n.66).

But the mere fact that other provisions of the Natural Gas Act may be available to the Commission to approximate the desired result hardly supports the argument that the Section 7(e) power is, therefore, not available. Ratemaking bodies are not bound "to the service of any single formula or combination of formulas. Agencies to whom * * * legislative power has been delegated are free, within the ambit of their statutory authority, to make the pragmatic adjustments which may be called for by particular circumstances." *FPC* v. *Natural Gas Pipeline Co.*, 315 U.S. 575, 586 (1942).

In addition, the majority's approach—permitting revenue crediting under Section 4 but not under Section 7—misconceives the differences between those sections. As Judge Wright observed (App. A, *infra*, 69a-70a):

> Section 4 has no magical property that affords the Commission greater powers than it otherwise would have. Rather, the main difference between the sections is that Section 4 is the mechanism for evaluating changes in the costs associated with already-certificated services, while Section 7 provides the mechanism for pricing and conditioning new services. Under Section 7 FERC has ample authority to ensure that certification of a new service—such as transportation—does not create an imbalance in the pipeline company's overall profit structure.

Moreover, the Section 4 procedures suggested by the majority are impractical. In order to impose a revenue crediting provision on a case-by-case basis either the Commission must wait for each pipeline company to file a Section 4 rate change,[9] or it must institute a Section 5 proceeding for each company. Both alternatives involve considerable delay and in-

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[9] The Commission has no power to fix rates under Section 4; it has only "the power to review rates and contracts made in the first instance by natural gas companies and, if they are determined to be unlawful, to remedy them." *FPC* v. *Hunt*, 376 U.S. 515, 522 (1964), quoting *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332, 341 (1956). Section 7, on the other hand, provides tested procedures which "act to hold the line awaiting adjudication of a just and reasonable rate." *Atlantic Refining Co.* v. *Public Service Comm'n of N.Y.*, *supra*, 360 U.S. at 392.

efficient use of staff resources. Indeed, this Court has more than once noted that the delays in Section 5 proceedings, where any remedy is prospective only, "appear[] nigh interminable." *Atlantic Refining Co.* v. *Public Service Comm'n of N.Y.*, *supra*, 360 U.S. at 389; *FPC* v. *Hunt*, 376 U.S. 515, 527 (1964). Similarly, to impose revenue crediting by a rulemaking under Section 4 of the Natural Gas Act is also a time-consuming undertaking. And until such time as revenue crediting provisions could be made effective under any of these alternative procedures, extra revenues currently being collected may escape any crediting requirement.

In short, the Commission's use of its Section 7 power to frame the revenue crediting provision in this case is simply an effort to formulate an "expeditious administrative method[]" (*Permian Basin Area Rate Cases*, 390 U.S. 747, 777 (1968)) that takes into account "*all* factors bearing on the public interest." *FPC* v. *Transcontinental Gas Corp.*, 365 U.S. 1, 8 (1961), quoting *Atlantic Refining Co.* v. *Public Service Comm'n of N.Y.*, *supra*, 360 U.S. at 391 (emphasis added by the Court in *Transcontinental*).[10]

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[10] The majority also held that, even assuming that the revenue crediting provision was within the ambit of the Section 7 conditioning power, nevertheless in this case use of the provision "was not supported by soundly based findings in the record * * *" (App. A, *infra*, 39a-41a).

We disagree. The Commission's position was, and is, that revenue crediting was required irrespective of the level of a pipeline's cost recovery under its Section 4 rates to its regular customers. Consequently, there was no need to make findings in the record as to the pipeline's revenues from its

2. The situation confronting the Commission in the revenue crediting case does not represent an isolated episode.[11] The need for a mechanism to credit unanticipated revenues recurs each time a pipeline enters into an arrangement (usually short-term) that was not taken into account at the time the rates were set. As gas companies must go further afield to obtain new supplies, there is a significant and growing need for pipelines to make transportation arrangements with other pipelines. In order to facilitate satisfying this growing need, the Commission recently promulgated regulations by which interstate pipelines may obtain blanket certificates, issued under Section 7(c) of the Natural Gas Act, authorizing them to transport gas for other interstate pipelines. 44 Fed. Reg. 68821 (1979) (to be codified in 18 C.F.R. 284.221(d)(1)). These regulations require net revenue crediting. In addition, as pipeline system supplies have ceased to increase or have decreased, the Commission has developed programs encouraging pipelines to transport gas for qualifying end users who buy

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regular customers' rates. If Panhandle's revenues are not adequate to meet its cost of service, it is free to file a rate increase under Section 4.

[11] The Commission's records show that the court of appeals' ruling affects three other cases filed in that court which feature revenue credit requirements: *Michigan Wisconsin Pipe Line Co.* v. *FERC*, C.A. No. 79-1349 (in abeyance pending outcome of the instant petition for a writ of certiorari); *Transcontinental Gas Pipe Line Co.* v. *FERC*, C.A. Nos. 79-1506, *et al.* (motion pending to hold proceeding in abeyance pending the outcome of the instant petition); *Northwest Pipeline Corp.* v. *FERC*, C.A. No. 78-2023 (on remand to the Commission in Docket No. CP77-378).

directly from producers.[12] Congress recently amended Section 7(c) of the Natural Gas Act to confirm the Commission's authority to approve such arrangements.[13] In short, all indications are that transportation arrangements of the type involved here will continue to be a significant feature of the natural gas pipeline industry.

Nor does the fact that Congress has enacted a new scheme dealing with natural gas (the Natural Gas Policy Act of 1978, Pub. L. No. 95-621, 92 Stat. 3350, 15 U.S.C. (Supp. II) 3201 *et seq.*) render the issues here of diminishing significance. The Natural Gas Policy Act provides for eventual deregulation of the *production* of most natural gas, but does not remove pipeline companies from regulation. In fact, in addition to its certification authority under Section 7 of the Natural Gas Act, the Commission has expanded power under Section 311 of the Natural Gas Policy Act to authorize transportation arrangements

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[12] See FPC Order No. 533, 54 F.P.C. 821 and 54 F.P.C. 2058 (1975), aff'd, *American Public Gas Ass'n* v. *FERC*, 587 F.2d 1089 (D.C. Cir. 1978); FERC Order No. 2, Docket No. RM75-25, issued February 1, 1978; FERC Order No. 27, Docket No. RM79-18, issued April 23, 1979. The programs established in FPC Order No. 533 and FERC Order No. 2 began as temporary measures; with passage of the Natural Gas Policy Act of 1978, they became permanent. See 15 U.S.C. (Supp. II) 3371. We are lodging copies of FERC Orders Nos. 2 and 27, which have not yet been reported, with the Clerk of the Court; copies of these orders are also being provided to counsel for respondent.

[13] Section 608 of the Public Utility Regulatory Policies Act of 1978, Pub. L. No. 95-617, 92 Stat. 3173, added 15 U.S.C. (Supp. II) 717f(c)(2).

and to impose conditions thereon. 15 U.S.C. (Supp. II) 3371.

It is not altogether clear what effect the majority ruling, if it is allowed to stand, would have on the Commission's conditioning power under Section 311 of the Natural Gas Policy Act. The Commission has adopted regulations utilizing this conditioning power to require revenue crediting in certain circumstances. See 44 Fed. Reg. 52185 (1979) (to be codified in 18 C.F.R. 284.103(d)(1)); 44 Fed. Reg. 30329-30330 (1979) (to be codified in 18 C.F.R. 284.205(b)(1)). While the majority declined to decide that issue in this case (see App. A, *infra*, 39a n.86), the ultimate logic of its ruling raises some doubt as to the crediting power under the Natural Gas Policy Act and, in any event, would seem to require cost tracking where revenue crediting is imposed.

3. As noted, the majority affirmed the Commission's order in the transportation cost case (C.A. No. 78-1960), and Panhandle has not sought review of that judgment in this Court. The majority, however, relied in part on the Commission's order in the transportation cost case in vacating the revenue crediting order which is the subject of this petition. It concluded that, even if revenue crediting was a permissible condition under Section 7(e) of the Natural Gas Act, the order imposing that condition would nevertheless have to be overturned because Panhandle was not allowed to offset its revenues by the costs of new transportation services (App. A, *infra*, 42a-44a). This ruling was erroneous.

By affirming the Commission's order in the cost tracking case, the majority acknowledged that, revenue crediting aside, a pipeline is not automatically entitled, absent Commission approval, to recover increased costs of one component of its cost of service (App. A, *infra*, 45a-49a). While the Commission has specifically provided for a purchased gas cost adjustment (PGA) provision by rulemaking under Section 4 (see 18 C.F.R. 154.38(d)(4)),[14] it has not adopted an automatic tracking provision for new (or increased) transportation costs.

There are sound reasons for the distinction. Contract transportation services are normally supplementary in nature, and their costs represent a relatively small portion of the average pipeline's total costs. Furthermore, when a pipeline arranges to obtain additional transportation services, its purpose is usually to bring new gas supplies into the pipeline system. In most cases, each dollar of new transporta-

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[14] Very special considerations prompted the Commission to adopt the PGA provision, as Judge Wright noted (App. A, *infra*, 58a-59a). Currently, the cost of purchased gas comprises about 75% of the cost of service of the average pipeline company. Due to shortages in gas supplies, changes in the cost of purchased gas are frequent and often substantial. Consequently, absent the PGA provision, pipeline companies would probably file frequent rate increases under Section 4 (see note 8, *supra*). Moreover, the PGA provision does not disturb the cost-revenue balance as established in the pipeline's approved base rates. There is generally a one-for-one relationship between a change in the pipeline's purchased gas costs and the consequent adjustment to the PGA charges paid by the customers. As we explain in the text, however, a transportation cost tracker may permit overrecovery of costs.

tion costs which the pipeline incurs is offset (in part or in whole) by additional fixed costs which the pipeline collects from the sale of additional volumes.[15]

Even in those cases where new transportation costs are not offset by new or excess revenues, the pipeline has no statutory right to be made whole by use of a cost tracker. Increased or unanticipated costs are an element of the business risk for which the Commission compensates a pipeline in its rate of return allowance. When a pipeline determines that the cost-revenue balance is no longer favorable, its remedy is to file increased rates under Section 4 of the Act.

While Judge Wright's concern for "[e]venhandedness" (App. A, *infra*, 79a) is understandable, it is mixing apples and oranges to conclude that a pipeline's dollar intake for providing one company with

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[15] Panhandle's transportation arrangement in C.A. No. 78-1960 is unusual, in that the additional fixed costs it collected from sale of new gas volumes did not entirely offset its new transportation costs. But Panhandle would not lose over $1.5 million per year on this particular transaction, as Judge Wright supposed (App. A, *infra*, 76a-77a). Judge Wright was relying on certain calculations made by Panhandle (*id.* at 77a n.30). However, Panhandle (and therefore Judge Wright) failed to take into account the fact that Panhandle's PGA clause would permit it to recover the increased cost of purchased gas. Thus, under the correct methodology (and otherwise making the same assumptions as Judge Wright), Panhandle would underrecover its fixed costs by about $600,000 annually. Moreover, since Panhandle in fact obtained a transportation cost tracker (through settlement) which went into effect no later than 6½ months after it began to incur new transportation costs in C.A. No. 78-1960 (see note 6, *supra*), Panhandle's total shortfall would be in the $300,000 range.

a new transportation service in one transaction should be netted against the pipeline's dollar outlay for obtaining a new transportation service from another company in a different transaction. The reason for not mixing together the costs and revenues of discrete transactions becomes clear when one contrasts their respective effects on the pipeline's overall cost-revenue balance.

Under revenue crediting, each dollar of net transportation revenues which the pipeline collects from a new transportation arrangement represents recovery of a dollar of costs which are already allocated to the pipeline's regular customers. By crediting transportation revenues to the customers' account, the pipeline is placed in a position no better and no worse than before it provided the service. By contrast, new transportation costs will normally be offset by the additional fixed-cost recovery from sales of the associated volumes. Were the pipeline in addition to obtain a cost tracker, the imbalance between its costs and its revenues would be still further aggravated.

For these reasons, the Commission acted properly when it permitted Panhandle to net against the revenues from its transportation service the "out-of-pocket" expenses it incurred *for the same service*, but did not allow Panhandle to net out the expenses it incurred in obtaining a *different* transportation service.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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MAY 1980

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 78-1356

PANHANDLE EASTERN PIPE LINE COMPANY,
PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT

No. 78-1630

PANHANDLE EASTERN PIPE LINE COMPANY,
PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT

No. 78-1960

PANHANDLE EASTERN PIPE LINE COMPANY,
PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT

Petition for Review of an Order of the
Federal Energy Regulatory Commission

Argued 23 April 1979

Decided 20 December 1979

Before: WRIGHT, *Chief Judge* and WILKEY, *Circuit Judge* and LARSON *, *United States Senior District Judge* for the District of Minnesota.

Opinion for the Court filed by *Circuit Judge* WILKEY.

Opinion concurring in part and dissenting in part filed by *Chief Judge* WRIGHT.

WILKEY, *Circuit Judge*: In these consolidated petitions, Panhandle Eastern Pipe Line Company (Panhandle) challenges orders issued by the Federal Energy Regulatory Commission (FERC). Two of these petitions [1] challenge FERC orders requiring Panhandle to flow through new transportation revenues to its resale gas customers via its unrecovered purchased gas account (PGA), while prohibiting the flow-through of new transportation costs. The third petition [2] challenges the Commission's selective waiver of its requirement of tracking authority allowing

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* Sitting by designation pursuant to 28 U.S.C. § 292(d).

[1] Nos. 78-1356 and 78-1960.

[2] No. 78-1630.

Panhandle to track decreased rates charged it by other pipelines, but not permitting it to pass on increased rates charged Panhandle. For the reasons to be discussed, we set aside the order in No. 78-1356, set aside in part and affirm in part the order in No. 78-1630, and affirm the order in No. 78-1960.

I. BACKGROUND

Commencing around 1971 shortages developed in the supplies of natural gas available to interstate pipelines, resulting in curtailment of deliveries to their customers. As a consequence of the reduction in pipeline gas supplies, natural gas users, including pipelines such as Panhandle, have had to seek more distant supplies of natural gas, which in turn requires special transportation arrangements in order to bring those supplies into their systems. A second consequence of the shortage and resulting curtailment has been that pipelines have substantial excess capacity which could be used, *inter alia*, to transport natural gas for other pipeline users. The instant petitions involve attempts by Panhandle and the Commission to grapple with problems arising from these changed conditions.

A. *No. 78-1356*

On June 30 1977 Panhandle and its wholly owned subsidiary, Trunkline Gas Company, filed a joint application pursuant to section 7(c) of the Natural Gas Act[3] for a certificate of public con-

[3] 15 U.S.C. § 717f(c) (1976).

venience and necessity to transport up to 1,800 Mcf of natural gas on a firm basis and 1,200 Mcf on a best efforts basis for eventual redelivery to Libby-Owens-Ford Company (LOF). The term of the transportation agreement was eight years. The rate proposed by Panhandle and Trunkline for the transportation service was $7,650 per month, subject to adjustment.

The Commission issued its order granting the requested certificates of public convenience and necessity for the transportation services on 16 December 1977. The certificates were granted for a two-year period only.[4] The Commission approved Panhandle's and Trunkline's proposed transportation charges, after a minor adjustment.

In the same order, the Commission stated:

> The rates in Docket No. RP 75-102 [Panhandle's 1975 rate case] provide for the recovery of all justifiable costs for gas to be sold or transported but do not include the transportation of gas as proposed herein. Since Panhandle will recover its costs through normal operations, any revenues from the instant transportation service shall be

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[4] The two-year limitation placed on the transportation service at issue here apparently reflects a Commission policy with respect to the transportation by jurisdictional pipelines of natural gas sold by certain producers from the onshore domain and the offshore nonfederal domain to nonresale industrial and commercial customers for high priority uses. *See* FPC Order No. 533, Docket No. RM75-25, *aff'd, American Pub. Gas Ass'n* v. *FERC*, 587 F.2d 1089 (D.C. Cir. 1978).

credited to its unrecovered purchased gas cost account.[5]

Thus in granting Panhandle's certificate to transport gas for LOF, FERC ordered the pipeline *to apply these transportation revenues to reduce the rates of gas resale customers by crediting the revenues to its PGA.*[6] This was designed to ensure that revenue gains of the transportation service would "inur[e] to the benefit of all of [Panhandle's] resale customers."[7]

On 13 January 1978 Panhandle requested a rehearing. It labeled the crediting requirement inappropriate because it was not limited to the excess of revenues over incurred costs. The company also argued that it was error to require crediting of transportation revenues to its purchased gas account because there is no relation between the two and "[t]he purchased gas account is carefully controlled under the Commission's PGA regulations, and should not be mixed up with transportation revenues." Further, there was no assurance the purchased gas adjustment tracking would be permitted throughout the eight-year period of the contract. Panhandle claimed the provision was discriminatory because it was not re-

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[5] *Panhandle E. Pipe Line Co.*, Docket No. CP77-479 (16 Dec. 1977), *modified* (22 Feb. 1978), *reprinted in* Joint Appendix (J.A.) at 50, 54.

[6] The mode of operation of the purchased gas account (PGA) provision is discussed at notes 69-72 and accompanying text *infra.*

[7] J.A. at 57, *see id.* at 61.

quired of another pipeline, Transco, in the transportation arrangement. Finally the company urged that the requirement was arbitrary because it required automatic crediting of revenues without provision for automatic recovery of transportation costs.[8]

The Commission rejected Panhandle's arguments in its order on rehearing issued 22 February 1978. FERC explained that the transportation service was made possible because of unused capacity in Panhandle's system, and that the costs associated with that capacity were already borne by Panhandle's resale customers. Thus, crediting the revenues through Account 191 was designed to benefit the resale gas customers who had paid for the costs associated with the excess pipeline capacity. There was no need to consider whether the PGA clause would continue the eight years of the contract because the certificate was limited to two years only. FERC found no discrimination vis-a-vis Transco, because Transco had previously agreed to credit transportation revenues to its unrecovered purchased gas account, and treatment of the revenues was an issue in certain Transco rate proceedings. The Commission did amend its 16 December 1977 order to allow Panhandle to recover its out-of-pocket costs incurred in performing the transportation services.[9] Finally, the Commission

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[8] *See* Application for Reconsideration and Rehearing, *re-*

[9] The amount to be credited to Account 191 each month, *printed in* J.A. at 69-71.

then, was the excess of revenues over jurisdictional out-of-pocket costs multiplied by the ratio of jurisdictional sales

pointed out that "[i]n the event Panhandle's other transportation costs [were] preventing it from earning a reasonable return, it [was] free at any time to submit a general rate change under Section 4(e) of the Natural Gas Act." [10]

On 20 April 1978 Panhandle filed its petition for review docketed as No. 78-1356.

B. *No. 78-1960*

On 25 October 1977 Trunkline applied for a certificate of public convenience and necessity to transport up to 10,000 Mcf of natural gas per day for Panhandle from offshore Louisiana. The gas was previously purchased by Panhandle from its affiliate Pan Eastern Exploration Company. The gas is transported by Trunkline to an existing interconnection with Panhandle near Tuscola, Illinois. Two other pipelines, Tarpon Transmission Co. and Tennessee Gas Pipeline Co., were also involved in the transportation arrangement. Panhandle was to pay $81,800 per month for the transportation service plus a proportionate share of Trunkline's payment to Tarpon for offshore transportation. Total cost to Panhandle for the new transportation service is claimed to be from $1.5 to 2 million per year.

Because the Commission had previously required Panhandle to credit new transportation revenues to

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volume to total sales volumes for the month. *Panhandle E. Pipe Line Co.*, Docket No. CP77-479 (order on rehearing, 22 Feb. 1978), *reprinted in* J.A. at 68, 70.

[10] *Id.* at 70.

its unrecovered purchased gas account, Panhandle petitioned to intervene in the proceeding and sought to have Trunkline's certificate conditioned so as to permit Panhandle's new transportation costs to be included as purchased gas costs recoverable through its PGA clause.[11]

On 17 April 1978 the Commission issued its order granting Trunkline's certificate and denying Panhandle's request.[12] The Commission explained that the crediting of transportation revenues was applied to short term transportation arrangements to "assure that the pipelines' customers share in the revenues received from such transportation service, since the rates that the customers pay are based on costs and revenues established in the pipelines' most recent approved rate case." The Commission then reasoned that recovery of transportation costs through the purchased gas adjustment provisions is not permitted unless the pipeline's tariff includes a "tracking" provision. Panhandle tariff does not include such a provision. Because the Trunkline proceeding concerned a long term transportation service (ten years), the Commission determined that "if the cost to Panhandle for the transportation service performed by Trunkline precludes earning a reasonable return, Panhandle should consider submitting a general rate change filing under Section 4(e) of the Act." The Commission further reasoned that since each Mcf of sales included fixed costs, to the extent Panhandle

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[11] *See* Petition for Intervention, *reprinted in* J.A. at 114-18.

[12] *Trunkline Gas Co.*, Docket No. CP78-43 (17 Apr. 1978), *reprinted in* J.A. at 119-26.

sold more gas than contemplated when the original rates were filed, the additional fixed costs recovered would offset the additional transportation costs.

Panhandle filed for rehearing on 16 May 1978.[13] In its appliction Panhandle strenuously objected to the crediting requirement previously imposed upon it in the LOF proceedings. The company argued that disallowing flow-through of costs in the Trunkline proceeding while requiring crediting of revenues in the LOF proceeding was inconsistent, and constituted a double penalty to Panhandle. It argued that the Commission's reliance on Panhandle's most recently approved rate case was misplaced, because it was "several years old and provide[d] no justification for the assumption that Panhandle's customers are paying for the costs presently being incurred." The company then requested a hearing to show that it was not recovering its costs of service and an adequate return. Panhandle argued that it was inconsistent for the Commission to require a "tracking" provision to pass on increased transportation costs, but not to pass on increased revenues. The company also objected to the requirement that it file a section 4 rate proceeding in order to recover its increased transportation costs, and cited two recent Commission cases where pipelines were allowed to track incremental costs without filing a section 4 rate increase. It also made reference to this court's decision in *Richmond Power & Light* v. *FERC*,[14] af-

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[13] Application for Rehearing, *reprinted in* J.A. at 127-32.

[14] 574 F.2d 610 (D.C. Cir. 1978).

firming a Commission order that did not require downstream electric utilities to absorb additional transmission costs. Finally, Panhandle maintained that the Commission erred in speculating that Panhandle's increased cost could be recovered through its increased sales, since the cost to Panhandle for the gas and transportation was greater than the highest rate it was allowed to charge.

The Commission denied the application for rehearing on 25 September 1978.[15] Again, it pointed out that if Panhandle's rates were inadequate to recover its costs, it should file for an increase under section 4. The Commission would not, however,

> permit Panhandle to include in Account No. 191, *Unrecovered purchased gas costs*, the costs incurred by it as a result of Trunkline's transportation of its gas. Such a course of action might have the effect of allowing Panhandle a rate increase when its rates, in the context of its *overall* cost of service *vis a vis* its *overall* revenues, might be fully adequate without such increase.[16]

While the Commission had "provided for tracking rate increases in the case of purchased gas costs in Order No. 452, . . . this did not extend to other cost elements, including transportation costs, such as are here sought by Panhandle." Although it prohibited the passing on of transportation costs, the Commission did not feel it improper to require flow-through of revenues via the PGA account "to prevent a pipe-

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[15] *Trunkline Gas Co.*, Docket No. CP78-43 (25 Sept. 1978), *reprinted in* J.A. at 135-39.

[16] *Id.* at 136.

line from being unjustly enriched at the expense of customers." In any event, the Commission stated that Panhandle's objections to the crediting provision should not be pursued collaterally "in this proceeding, where they are of peripheral interest only."

The Commission distinguished the two cases that were cited by Panhandle as inconsistent with the Commission's refusal to allow the company to track its increased transportation costs. Those two cases involved tracking of storage costs, and were to be limited to their unique facts. The Commission then distinguished *Richmond Power* on two grounds: (1) it was a negotiated settlement, and (2) it "involved a coordinated response by many utilities to a special emergency situation at the behest of a stated Commission policy." In response to Panhandle's request for a hearing to show that it was not recovering its costs, the Commission stated that the company was "free in these circumstances to file a rate increase pursuant to Section 4 of the Natural Gas Act at any time."

Panhandle filed a peition for review, No. 78-1960, on 28 September 1978, which was consolidated with Nos. 78-1356 and 78-1630 by order of the court on 3 October 1978.

C. *No. 78-1630*

The orders under review in No. 78-1630 concern two rate adjustment filings by Panhandle. The first grew out of a Commission certificated joint trans-

portation service [17] wherein gas purchased by Northern Natural Gas Co. (Northern) in offshore Louisiana was transported by Stingray Pipeline Co. (Stingray), Natural Gas Pipeline Co. of America (Natural), Trunkline, and Panhandle for eventual redelivery to Northern. Because of the location of delivery and redelivery points of the gas, there is no actual transportation by Panhandle and therefore no additional charge for its services. Pursuant to Panhandle's FERC Rate Schedule T-18, Northern pays Panhandle a monthly charge representing the total transportation charges of Stingray, Natural, and Trunkline. Panhandle in turn pays to Trunkline the identical amount, pursuant to Trunkline's FERC Rate Schedule T-20. Thus, as to transportation charges payable by Northern, Panhandle appears to be simply a conduit between Northern and Trunkline.

On 6 February 1978 Panhandle filed a proposed rate change for Northern.[18]. In its cover letter, Panhandle referenced only a decrease in Trunkline's transportation rates, but the attached worksheet made clear that the proposed change reflected a significant increase in the charge to Northern based on a higher rate to be paid Stingray.

The second filing,[19] submitted 9 February 1978, involved a Commission approved transportation service

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[17] *Northern Natural Gas Co.*, Docket No. CP77-450 (30 Sept. 1977), *reprinted in* J.A. at 72-76.

[18] *Reprinted in* J.A. at 79-83. Docketed at No. RP78-39.

[19] *Reprinted in* J.A. at 84-90. Docketed at No. RP78-40.

by Trunkline and Panhandle for Central Illinois Public Service Co. (CIPSCO).[20] Panhandle's cover letter referenced Trunkline's general rate decrease, and the tariff sheets reflected only that rate increase.

On 10 March 1978 the Commission by letter order accepted the proposed rate decrease as to CIPSCO, but rejected the increase as to Northern.[21] The Commission explained that Panhandle did not have tracking authority to reflect the rate changes, but the CIPSCO adjustment would be accepted anyway, since the proposed rate was equal to or lower than currently effective rates. The increased rate for Northern was rejected for lack of tracking authority.

Panhandle applied for a rehearing on 10 April 1978.[22] It contended that the rates and charges contained in the revised tariff sheets were obligatory under Panhandle's Rate Schedule T-18, were approved by prior Commission order, and therefore not subject to partial approval and partial rejection without any evidentiary basis, hearings, procedural safeguards, or finding supporting such action. The pipeline argued that it was improvident and erroneous to deny Panhandle's proposed increase when the Commission had approved Trunkline's application for the identical amount. Panhandle submitted that it was

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[20] *Panhandle E. Pipe Line Co.*, Docket No. CP77-47 (19 Aug. 1977).

[21] *Panhandle E. Pipe Line Co.*, Docket No. CP77-39 *et al.* (10 Mar. 1978), *reprinted in* J.A. at 91-92.

[22] Application for Reconsideration and Rehearing *reprinted in* J.A. at 93-97.

error for the Commission to waive its requirement of tracking authority to permit filing of rate reductions, and at the same time refuse to waive them as to rate increases. Panhandle pointed out that it would suffer a significant out-of-pocket loss unless it were permitted to pass through the increased. charges.

The Commission denied the application for rehearing on 9 May 1978.[23] It explained that Panhandle had no authority under its transportation certificate to track changes in its rates, and that the acceptance of Trunkline's related rate increase did not automatically entitle Panhandle to an increase. Trunkline's rate change, in accordance with regulations, was supported by cost-of-service evidence, which Panhandle's was not. That the increased transportation charge to Panhandle had been approved by the Commission did not entitle the company to pass on the increases in the absence of an approved tracker or a cost-of-service showing. The Commission held that it had discretion to accept the voluntarily filed rate decrease to benefit consumers, and to reject simultaneously a rate increase. It stated that waiver of its requirements is appropriate for good cause shown, but that Panhandle had not made such a showing in this case.

Panhandle filed its petition for review as to these orders on 6 July 1978.

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[23] *Panhandle E. Pipe Line Co.*, Docket No. RP78-39 *et al.* (9 May 1978), *reprinted in* J.A. at 99-103.

II. The Merits

It is hard to resist agreeing with Panhandle that the orders under review appear in various ways to put the squeeze on the pipeline, although to be sure the existence and degree of any pinch depends on which of several states of the world actually exists. In general, the Commission appears to take a quite liberal view of its own authority to require the flow-through of revenues, while imposing rather vigorous procedural standards on Panhandle in its effort to recover its additional costs. Whether the various procedures were valid or fair is a rather close question. Nevertheless, we think that the revenue crediting requirement in No. 78-1356 must be set aside as unauthorized by section 7, violative of Commission regulations, not premised on solidly based findings in the record, and unreasonable. Since Panhandle's objections to the Commission's order in No. 78-1960 relate largely to its inconsistency with the revenue crediting policy, the arguments are in great measure defused by our disposition of No. 78-1356. To the extent Panhandle is claiming to be entitled to recover increased transportation costs via Account 191, even in the absence of revenue crediting, we affirm the Commission's refusal. As to No. 78-1630, we think that when a pipeline is merely an accounting conduit for charges made by other pipelines, a proper case for waiver is presented. We therefore set aside that portion of the order disallowing Panhandle the right to track its increased cost, while affirming that portion approving the filing of decreased rates.

A. *No. 78-1356*

Panhandle contends in No. 78-1356 that the requirement that it credit its transportation revenues to Account 191, especially when it is prohibited from charging its transportation costs similarly, (1) violates section 5 of the Act, (2) runs roughshod over the Commission's regulations concerning the PGA clause, and (3) is in various ways unfair, discriminatory, and contrary to cost precedent. The Commission counters that it is authorized under section 7 to impose such conditions on certificates, that the condition was necessary to prevent overcollection by Panhandle of fixed costs, and that the order violated neither Commission regulations nor precedent.

Although the objective of the Commission in fashioning the revenue crediting requirement may be laudable, the order must be set aside because we conclude that the Commission's section 7 conditioning power does not authorize the adjustment of rates charged customers not receiving the services to be certificated. We also find that the order violates the Commission's accounting regulations, does not rest on soundly based findings in the record and is unreasonable. Since we reverse on these ground we do not find it necessary to reach Panhandle's contention that the order was discriminatory or contravened precedent.

1. *Section 7 Authority*

(a) Ratemaking Under the Natural Gas Act

The purpose of the Natural Gas Act was to "underwrite just and reasonable rates to the consumers of natural gas." [24] It was framed "to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges," [25] and at the same time, to ensure that rates set be "consistent with the maintenance of adequate service in the public interest." [26]

Three interrelated sections constitute the "comprehensive and effective regulatory scheme" [27] Congress created with regard to ratemaking. Section 7 provides that to undertake the "transportation or sale of natural gas," an entity must first obtain "a certificate of public convenience and necessity issued by the Commission." [28] In issuing such certificates,

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[24] *Atlantic Ref. Co.* v. *Public Serv. Comm'n*, 360 U.S. 378, 388 (1959) (citing *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944)).

[25] *Id.*

[26] Natural Gas Act § 7(c), 52 Stat. 821, 825 (1938) (current version at 15 U.S.C. § 717r(c) (1976)). The deletion of this language by the 1942 amendment to § 7 was not intended to change this congressionally declared purpose. *See Hearings Before the House Interstate and Foreign Commerce Comm. on H.R. 5249*, 77th Cong., 1st Sess. 18-19. *See generally* H.R. REP. No. 1290, 77th Cong., 1st Sess. (1941); S. REP. No. 948, 77th Cong., 2d Sess. (1942).

[27] *Panhandle E. Pipe Line Co.* v. *Public Serv. Comm'n*, 332 U.S. 507, 520 (1947).

[28] 15 U.S.C. § 717f(c) (1976).

the Commission has "the power to attach . . . such reasonable terms and conditions as the public convenience and necessity may require." [29] Once rates are authorized under section 7, a natural gas company may file for an increase under section 4.[30] The company must file its rates thirty days before they go into effect.[31] The Commission may then suspend the new rate schedule for five months.[32] Thereafter the increased rates may be collected but the Commission may require a bond to ensure refunds of "increased rates or charges by its decision found not justified." [33] The burden of proof in section 4 proceedings is on the natural gas company.[34]

On the other hand, if rates are unjust or unreasonable, the Commission may adjust them pursuant to section 5.[35] This section provides that "[w]henever the Commission, after a hearing . . . shall find that any rate . . . is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate . . . and fix the same by order." [36] Section 5 rate adjustments

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[29] *Id.* § 717f(e).

[30] *Id.* § 717c.

[31] *Id.* § 717c(d).

[32] *Id.* § 717c(e).

[33] *Id.*

[34] *Id.*

[35] *Id.* § 717d.

[36] *Id.* § 717d(a).

may be prospective only,[37] and the Commission may not order rate increases unless the company has filed a new rate schedule.[38]

In the instant case, the Commission has attempted to effectuate the policies of the Natural Gas Act by mandating a flow-through of revenues to resale customers as a condition on a section 7 transportation certificate. The Commission has implicitly determined that permitting Panhandle to retain these transportation revenues would allow it to be "unjustly enriched at the expense of consumers."[39] Since theoretically Panhandle is already recovering from rates set in a prior rate settlement the fixed costs of the unused capacity that permits it to provide transportation services, "additional revenues covering the same fixed costs" are overcollections.[40]

Panhandle claims that if in fact the Commission believes its rates are too high, it must follow the customary procedures under section 5 of the Act which permits it to act only "after hearing" and only after a finding that Panhandle's overall rates are unjust.[41] The Commission argues that since the reve-

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[37] *Atlantic Ref. Co.* v. *Public Serv. Comm'n*, 360 U.S. 378, 389 (1959).

[38] 15 U.S.C. § 717d(a) (1976).

[39] *Trunkline Gas Co.*, Docket No. CP78-43 (25 Sept. 1978), *reprinted in* J.A. at 136 (explaining basis of revenue crediting in the instant order).

[40] Brief for Respondent at 28.

[41] Brief of Petitioner at 34.

nue crediting condition was imposed pursuant to the Commission's section 7 power, section 5 requirements of hearings and findings do not apply.[42]

The underlying premise of the Commission's argument is that it had authority under section 7 to condition the certificate to require revenue crediting, so long as the condition was "supported by soundly based findings in the record" and was reasonable.[43] We do not interpret section 7 so expansively.

(b) *The Scope of the Section 7 Conditioning Power*

The actual language of section 7(e) is broad indeed. It states that in granting certificates: "The Commission shall have the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require." In the absence of sections 4 and 5 of the Act, this broad mandate conceivably could authorize adjustment of rates not involved in the actual certificate proceeding. But section 7's broad conditioning power must be read in conjunction with sections 4 and 5. In that context, for three reasons we believe that the conditioning power does not extend to adjusting previously approved rates for services not before the Commission in the relevant certificate proceeding.

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[42] Brief for Respondent at 28-30.

[43] *Id.* at 17-22.

(i) *Emasculation of the Role of Section 5*

First, the more expansive reading would effectively emasculate the role of section 5 in the ratemaking scheme. Any time the Commission had good reason to believe that a pipeline's rates were unjust or unreasonable, it could simply condition the granting of new certificates on the adjustment of those rates, the condition to terminate only when the pipeline filed a new rate proceeding under section 4. There would be no need for the Commission to use section 5 so long as pipelines continued requesting new certificates—instead, the Commission could simply condition certificates on rate reductions and shift the burden to the pipelines to show affirmatively that its previous rates continued to be just and reasonable. Section 5 would be reduced to a stopgap device, necessary for reducing unjust or unreasonable rates only when no new certificate filings were being made. We do not think that section 7 was meant to reduce so sharply the role of section 5, and therefore decline to adopt FERC's expansive interpretation of the conditioning power.[44]

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[44] One could, of course, take a more limited view of the scope of § 7(e) than does the Commission, and still sustain the disputed order. The narrower construction would provide that the strictures of § 5 could be avoided by revenue crediting only when unanticipated and relatively cost-free revenues are to be received by a pipeline from certificated services. Such an interpretation might not emasculate the role of § 5 so fully as does FERC's broad construction, and would still support revenue crediting in this case. But expanding the scope of § 7 in this more limited fashion would still significantly

(ii) *Erosion of Protections Against Regulatory Lag and Rate Instability*

Although the Act's principal purpose is to protect consumers against excessive rates, a corollary purpose is to allow natural gas companies their cost of service and a reasonable rate of return.[45] Recognizing that it is in the public interest that companies receive adequate revenues to maintain high quality service, Congress designed sections 4 and 5 to protect companies against regulatory lag[46] and provide a degree of certainty in their rate schedules. Under section 4, once a company has filed a new rate schedule and the five-month statutory suspension period has elapsed, the rates go into effect—subject to a refund obligation. Thus, should administrative proceedings take longer than five months companies are protected against additional loss of revenues. Once rates are approved by certificate or in section 4 proceedings, the Commission may change them only after a section 5 hearing and specific findings that they are unjust

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erode the role of § 5, and additionally dilute protections of §§ 4 and 5. *See* notes 45-52 and accompanying text *infra*. The line must be drawn somewhere, and for reasons to be discussed we think the price adjustment powers of § 7(e) do not extend to previously approved rates for sales or services not before the Commission in the certification proceeding.

[45] *See* note 26 *supra*.

[46] *Algonquin Gas Transmission Co.* v. *FPC*, 534 F.2d 952, 956 (D.C. Cir. 1976) (referring to § 4 protections).

or unreasonable.[47] Section 5 rate reduction orders may be prospective only. This ensures rate stability; companies may count on receiving previously approved revenues without the threat of an indefinite refund requirement at a later date.

Interpreting the conditioning power to allow adjustment of previously approved rates eliminates both protections in one fell swoop. Rate stability is destroyed because at any time a certificate is filed, immediate reductions may be ordered as to previously approved rates. Protections against revenue loss caused by administrative delay are seriously diluted. In addition to the thirty-day filing period and five-month rate suspension period prescribed by the Act, a pipeline would be deprived of the revenues from previously approved rates during the time necessary to prepare new section 4 filings.[48] Because the Com-

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[47] *See Atlantic Ref. Co.* v. *Public Serv. Comm'n*, 360 U.S. 378, 389, 392 (1959); *Colorado Interstate Gas Co.* v. *FPC*, 142 F.2d 943, 954 (10th Cir. 1944), *aff'd*, 324 U.S. 581 (1945); *cf. Sierra Pac. Power Co.* v. *FPC*, 223 F.2d 605, 607 (D.C. Cir. 1955) (under § 206 of Federal Power Act—virtually identical to § 5 of Natural Gas Act—a finding of unreasonableness is prerequisite to Commission modification of filed rate), *aff'd*, 350 U.S. 348 (1956). Of course, the Commission could also alter rates upon the company's making a new § 4 filing.

[48] Preparation for new § 4 filings apparently can be time consuming. If FERC's interpretation of § 7 were correct, to eliminate loss of revenues between the time of certificate grant and § 4 proceedings, a natural gas company could prepare a "defensive" filing before seeking new certificates. We decline to force companies, when seeking transportation

mission's expansive view of the conditioning power would largely extinguish these protections of sections 4 and 5, we refuse to adopt it.

(iii) *Circumvention of Section 5 Requirements of Hearings and Findings*

Finally, we reject the broad interpretation of section 7 because it allows circumvention of section 5 requirements of a hearing and specific findings as to justness and reasonableness of existing rates. The law seems clear that once rates are approved in certificates or rate proceedings, they may only be adjusted by the Commission after a finding that they are unjust, unreasonable, or not the lowest reasonable rate.[49] It would be ironic after rates have been approved as theoretically just and reasonable under section 4 to allow the Commission to reduce them by revenue crediting or other means without a specific finding that the rates are no longer just and reasonable.[50] We therefore decline to adopt the wider

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or other certificates, to choose between preparing massive rate filings beforehand or risking additional revenue loss during the preparation of new § 4 filings after imposition of a revenue crediting requirement.

[49] *See* note 47 *supra*.

[50] It may not be quite so unseemly to condition a certificate on reduction of other rates previously certificated but not yet approved as just and reasonable. That question is not before us. The rates here reduced had previously been approved by the Commission in *Panhandle E. Pipe Line Co.*, Docket No. RP75-102.

construction of section 7 that would do away with the section 5 requirement of hearings and findings before reducing rates.[51]

For these reasons we hold that FERC may not as a condition on a section 7 certificate require a pipeline to adjust rates previously approved by the Commission for customers not receiving the services to be certificated.[52]

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[51] An argument could be made that the condition before us would be permissible under §§ 5 and 7 if imposed after an appropriate hearing and findings. The Commission could consider the justness and reasonableness of a pipeline's rate structure in light of new revenues as part of the certificate hearing required by § 7(e), and enter proper findings before mandating revenue crediting. Since the Commission did not follow such a procedure here, the question is not squarely before us, and we do not rule on it. We do, however, doubt the practical utility of such a hybrid device. Once the hearing and finding requirements of § 5 are met, there is no need to impose rate reductions by certificate condition, it may be done in a straightforward manner under § 5.

[52] Judge Wright attempts to "quickly dispose[]" of the serious issues raised by the Commission's § 7 order by claiming that rates are not adjusted at all. He claims that "[*r*]*ates* are not adjusted; only the size of future rate changes via the purchased gas account is affected." Concurring and Dissenting Opinion at 13-14. This is a difference without a distinction. Under the Commission's order, new transportation revenues are placed in Account 191 (the unrecovered purchased gas account) to be offset against any gas price increases or aggregated with price decreases. When the subsequent six-month purchased gas adjustment order issues, the net result is a lower rate than that which resale customers would otherwise pay. *It is this tinkering with previously approved rate schedules for resale customers that we find objectionable.*

We think it fair to say that a focal point of our disagreement with Judge Wright is the proper characterization of the

(c) *Case Law.*

The Commission cites a great many cases to show the "considerable breadth" of its conditioning authority under section 7(e). The decisions are distinguishable from the case at hand, and we do not find them controlling.

FERC initially cites the Supreme Court's seminal opinion in *Atlantic Refining Co.* v. *Public Service Commission (CATCO).*[53] There, the Court declared that the Commission should give "a most careful

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revenue crediting order. He views the essence of the challenged order as "govern[ing] the use of revenues generated from a new service." *Id.* at 8. Because the pipeline's rate of return arguably is the same after revenue crediting as it was before any transportation revenues were received, Judge Wright suggests that § 5 is not emasculated, protections against regulatory lag and rate instability are not eroded, and the hearing and finding requirements of § 5 are not circumvented. *Id.* at 13-14. He submits that here the Commission has used its § 7 powers to "hold the line" on Panhandle's rate of return. *Id.* at 13.

In our view, *the essence of the Commission's order is the adjustment of previously approved rates to reach the regulatory end of preventing any increase in Panhandle's profits (or mitigation of losses) from receipt of new transportation revenues.* Assuming this questionable regulatory objective to be valid, we believe *the means of implementing it used by the Commission is impermissible.* While the Commission may consider a pipeline's rate of return in setting prices for certificated services, we do not believe FERC may order changes in other, previously approved, rates in the name of preventing a possible increase in the rate of return. Allowing the Commission to do so—even when the rate reductions are limited by the amount of revenue credited—significantly undercuts the policies of §§ 4 and 5 as we have here outlined.

[53] 360 U.S. 378 (1959).

scrutiny and responsible reaction to *initial price proposals* of producers under § 7." [54] The Court noted that the interminable delay involved in section 5 proceedings, "the fact that the Commission was not given the power to suspend initial rates under § 7," and the absence under section 5 of a refund protection make "it the more important . . . that 'this crucial sale should not be permanently certificated unless the rate level has been shown to be in the public interest.' " [55] Without appropriate rate conditions in the certificate, "a windfall for the natural gas company with a consequent squall for the consumers" could result. The Court found that "[t]his the Congress did not intend." [56]

The Court continued,

> There is, of course, available in such a situation, a method by which the applicant and the Commission can arrive at a rate that is in keeping with the public convenience and necessity. The Congress, in § 7(e), has authorized the Commission to condition certificates in such manner as the public convenience and necessity may require. Where the proposed price is not in keeping with the public interest because it is out of line or because its approval might result in a triggering of general price rises or an increase in the applicant's existing rates by rea-

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[54] *Id.* at 391 (emphasis added).

[55] *Id.* at 389-90 (quoting *Continental Oil Co.*, 17 F.P.C. 563, 575 (1957)).

[56] *Id.* at 390.

> son of "favored nation" clauses or otherwise, the Commission in the exercise of its discretion might attach such conditions as it believes necessary.[57]

The Court noted that in allowing the Commission to attach rate conditions on certificates, "§ 7 is given only that scope necessary for 'a single statutory scheme under which all rates are established initially by the natural gas companies . . . subject to being modified by the Commission.' " [58] Further, "[s]ection 7 procedures in such situations thus act to hold the line awaiting adjudication of a just and reasonable rate." [59]

The other decisions cited us generally expand or refine this section 7(e) conditioning power regarding rates and contractual provisions for the services to be certificated.[60] As to rate conditions, the decisions

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[57] *Id.* at 391.

[58] *Id.* at 392 (quoting *United Gas Pipe Line Co.* v. *Mobile Gas Serv. Corp.*, 350 U.S. 332, 341 (1956)).

[59] *Id.*

[60] *United Gas Improvement Co.* v. *Callery Properties, Inc.*, 382 U.S. 223, 229-30 (1965) (where reviewing court find that unconditional permanent certificate permitted excessive rate, Commission on remand may condition certificate to require refunds for period company sold gas at prices exceeding those properly determined to be in public interest); *FPC* v. *Hunt*, 376 U.S. 515 (1964) (Commission may condition temporary certificate on maintenance of prescribed price during period of temporary authorization, § 4 procedures to change rates become applicable at time of permanent or unconditioned temporary certification); *Algonquin Gas Transmission Co.* v. *FPC*, 534 F.2d 952, 955-57 (D.C. Cir. 1976)

accord with the principle that *section 7 may be used "to hold the line awaiting adjudication of a just and reasonable rate."* [61]

Here, the Commission has not acted just to hold the line on certificated rates, but to adjust other, previously approved rates as well.[62] FERC has not

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(§ 7 rate conditions offer mechanism to "hold the line" on initial rates until regular rate setting provisions of the Act come into play); *Consumer Fed'n of America* v. *FPC*, 515 F.2d 347, 356 (D.C. Cir.) (preservation of statutory scheme depends on diligent enforcement of § 7 certification requirement as a holding operation on initial rates), *cert. denied*, 423 U.S. 906 (1975); *Public Serv. Comm'n* v. *FPC*, 543 F.2d 757, 823 (D.C. Cir. 1974) (data that Commission, pursuant to § 7, may order pipeline to flow through to customers rate reductions and refunds by producers), *cert. denied*, 424 U.S. 910 (1976); *California Oil Co.* v. *FPC*, 315 F.2d 652, 655-57 (10th Cir. 1963) (Commission has power to set "in-line" price as certificate condition); *Pure Oil Co.* v. *FPC*, 292 F.2d 350, 352-53 (7th Cir. 1961) (authority to set initial sales prices when supported by soundly based findings in the record); *Texaco Inc.* v. *FPC*, 290 F.2d 149, 154-55 (5th Cir. 1961) (power to set initial prices).

[61] *CATCO*, 360 U.S. at 392 (emphasis added); *see, e.g.*, *Algonquin Gas Transmission Co.* v. *FPC*, 534 F.2d 952, 955 (D.C. Cir. 1976); *Consumer Fed'n of America* v. *FPC*, 515 F.2d 347, 356 (D.C. Cir.), *cert. denied*, 423 U.S. 906 (1975).

[62] Chief Judge Wright suggests that because FERC's order is intended to leave Panhandle's "rate of return at exactly the same level as before the order," it is a "classic" example of use of the § 7 conditioning power to "hold the line" pending a full cost-of-service proceeding. Concurring and Dissenting Opinion at 13. However, the classic use of § 7 is to "hold the line" on *rates* not rates of return. *See* notes 59-61 and accompanying text *supra*. We are not aware of, and Judge Wright does not refer to, any case approving FERC adjustment in § 7 proceedings of rates not before it with the objective of "holding the line" on the rate of return.

cited, and our own research does not disclose, any judicial authority holding that the Commission may tinker with rates previously found just and reasonable in conditioning a certificate dealing with other sales or services. For the reasons already mentioned, we decline to so extend the Commission's conditioning powers.

In addition, we note that the considerations mandating the use of section 7 to set initial rates for certificated sales or services do not require its use to adjust previously approved rates for other services. As the Supreme Court noted in *CATCO*, when initial rates are set the only protection consumers have against excessive rates, other than the Commission's section 7 scrutiny of proposed rates, is the possibility of a subsequent section 5 proceeding to lower rates.[63] The delay, lack of suspension power, and lack of power to order retroactive relief in section 5 proceedings make it important for the Commission to "hold the line [by certificate condition] awaiting adjudication of just and reasonable rates."[64] Here, just and reasonable rates have already been adjudicated, at least by settlement approved by the Commission. The resale customers have had the protection of a section 4 proceeding with its refund and suspension provisions, and as well have continuing protection of section 5, inadequate though it may be of itself. The rates have already been approved as

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[63] *See* 360 U.S. at 392.

[64] *Id. See note* 55 and accompanying text *supra*.

theoretically just and reasonable, and therefore the spectre of "a windfall for the natural gas company with a consequent squall for the consumers" is not so ominous in the absence of certificate conditioning, as it is where initial rates are proposed. Since the public interest here seems to be adequately protected by sections 4 and 5, we do not feel that the cited cases require us to extend the scope of section 7 to allow adjustment of previously approved rates for services not involved in the pertinent certificate proceeding.

(d) *Conclusion as to Section 7 Authority*

Because we believe a contrary interpretation would emasculate the role of section 5, dilute the protections provided in sections 4 and 5 against regulatory lag and rate instability, and eliminate section 5 protections of hearing and specific findings as to justness and reasonableness of rates prior to a rate reduction order, and in the absence of binding contrary precedent, we hold that the Commission does not have authority under section 7 to compel flow-through of revenues to customers of services not under consideration in that proceeding for certification.[65]

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[65] We think Chief Judge Wright tacitly agrees with us when he states that "*Section 4* is the mechanism for evaluating changes in the costs associated with *already certificated services*, while *Section 7 provides the mechanism for pricing and conditioning new services.*" Concurring and Dissenting Opinion at 15 (emphasis added). This dichotomy drawn in his opinion strongly supports our conclusion that a § 7 proceeding is not the appropriate occasion for adjustment of previously approved rates not then before the Commission.

In so doing, we do not mean to intimate that FERC may not take a company's overall rate structure into consideration in issuing certificate orders. It may evaluate that and myriad other factors as they bear on the public convenience and necessity. The Commission may not, however, order adjustments in previously approved rates for services not before it in the certificate proceeding.

We recognize that there may be instances where certification of essentially cost-free transportation services will push a company's rate of return over the just and reasonable level. Nevertheless, we do not believe the solution to the problem is to ignore the policies and protections of sections 4 and 5 and forbid companies to keep revenues pending a section 4 filing. We think a more acceptable and equitable solution would be the adoption by the Commission in appropriate proceedings [66] of some sort of "tracker" system for transportation revenues and costs similar to the PGA clause.[67] A tracker system would avoid

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[66] For instance, the Commission might begin approving tracking clauses in individual § 4 proceedings, or it might by rulemaking adopt a policy allowing inclusion of such clauses in rate filings under § 4.

[67] Judge Wright suggests that it is more appropriate to decide whether costs and revenues associated with new services should be "flowed through" at the time of their certification proceeding than to require the existence of a tracking provision as a prerequisite. Concurring and Dissenting Opinion at 10 n.18. We think that the proper time to decide what factors will affect approved rates is at the time they are set, not afterward. Once rates and rate adjustment mecha-

the infirmities of the Commission's order here—it would not eliminate the role of section 5, it would avoid revenue loss caused by administrative lag and provide rate stability, and it would not run afoul of the section 5 policies of hearings and findings. Further, such a tracker would allow resale customers to receive the benefits and bear the burdens of transportation services provided by and for other companies. We cannot force the Commission to adopt such a system, but today's holding certainly should not be viewed as precluding use of transportation tracking clauses as approved in appropriate proceedings.[68]

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nisms have been approved in a § 4 proceeding, we do not think the Commission has power to further adjust them in a subsequent § 7 proceeding certificating a new service.

[68] Thus, we cannot agree with Judge Wright's implication that our disposition of Nos. 78-1356 and 1960 "effectively prevent[s] the Commission from adopting expeditious proceedures altogether" for dealing with changes in various costs and revenues occurring between § 4 proceedings. Concurring and Dissenting Opinion at 9. Our disposition leaves open the option of adoption of tracking clauses similar to the PGA provision to handle interim changes of transportation costs and revenues. A more novel solution where no tracking provision exists would be for the Commission to approve the transportation services subject to a "cross-refund" to Panhandle's customers in the event a subsequent ratemaking disclosed that its rates had been unjust or unreasonable. We note that such a procedure would not emasculate the role of § 5, engender administrative delay and consequent revenue loss, nor eliminate hearings and findings as to justness and reasonableness of rates in the administrative process. *In addition, a refund condition would have the advantage of imposing no irretrievable loss on the company or the con-*

2. *Violation of Commission Regulations*

The purchase gas adjustment clause provisions [69] were adopted by the Commission to "permit pipeline companies to protect themselves against supplier rate increases." [70] The clause allows pipelines to adjust their rates semi-annually to reflect changes in unrecovered purchased gas costs. In the meantime, purchased gas costs above or below the current adjustment are placed in a deferred account (Account 191), to be recovered over the next six-month period as a surcharge to the rates, or in the case of lower costs, a reduction in the rates.[71] This relieves pipelines of the burden of continuous rate filings, enabling them to recover expeditiously "the cost of pur-

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sumer. There is a possibility that the "cross-refund" condition somehow might run afoul of the implied proscription of retroactive relief in § 5; whether that of itself would invalidate the procedure is an issue we do not decide.

[69] Chief Judge Wright suggests that in this section we tacitly endorse the PGA regulations, and claims that this is inconsistent with our holding that revenue crediting is unauthorized by § 7. Concurring and Dissenting Opinion at 10 n.19. We think that revenue crediting as here imposed and the PGA provisions are distinguishable. The Commission ordered revenue crediting under its purported § 7 *authority*; the PGA mechanism must be adopted and approved at a § 4 *proceeding* before any price adjustment may be made. To what extent the PGA regulations "alter the statutory scheme," *id.* at 10 n.19, if any, and whether any such "alteration" is permissible under § 4, are issues not presented in this appeal, and we do not decide them.

[70] Order No. 452, 47 F.P.C. 1049, 1050 (1972).

[71] 18 C.F.R. § 154.38(d)(4) (1979).

chased gas [which] constitutes the largest single component of their cost of service." [72]

The unrecovered purchased gas cost account is Account 191 of the Uniform System of Accounts for Natural Gas Companies. It provides:

> 191 Unrecovered purchased gas costs.
>
> A. This account shall include purchased gas costs related to Commission approved purchased gas adjustment clauses when such costs are not included in the utility's rate schedules on file with the Commission.[73]

The pertinent regulation defines "purchased gas cost" as

> the cost of wellhead purchases, field line purchases, plant outlet purchases, transmission line purchases, and pipeline production from leases acquired on and after October 7, 1969. Noncon-current exchange transactions may be reflected as a cost of purchased gas.[74]

Panhandle points out that these regulations nowhere permit inclusion of transportation costs or revenues. It argues that the subject revenues should instead be credited to Account 489, titled "Revenues from transportation of gas for others." [75]

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[72] Order No. 452, 47 F.P.C. 1049, 1050 (1972).

[73] 18 C.F.R. § 201 (1979).

[74] 18 C.F.R. § 154.38(d) (4) n.1 (1979).

[75] 489 Revenues from transportation of gas of others.

This account shall include revenues from transporting gas for other companies through the production, trans-

Panhandle also argues that the challenged order violates longstanding Commission precedent and lists a number of cases where the Commission has refused to allow inclusion of transportation costs in a PGA clause.[76] FERC distinguishes these decisions on the basis that they involved pass-through of costs, not revenues.[77] To demonstrate that the order under review is in accord with Commission precedent, it cites a number of recent orders, none judicially reviewed, in which it has ordered crediting of transportation revenues.[78]

Thus the Commission's position seems to be that the PGA regulations allow pass-through of transportation revenues, but not of costs. We do not read the carefully constructed purchased gas regulations so loosely. Account 191 applies to *costs*, not *revenues*, and to *purchased gas* items, not *transportation* items. Moreover, Account 489 by its terms appears to be the proper locus for transportation revenues.

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mission, and distribution lines, or compressor stations of the utility.

18 C.F.R. § 201 (1979).

[76] *See* Brief of Petitioner at 42. In its order denying rehearing in No. 78-1960, affirmed by us today, *see* Part II B *infra*, the Commission stated that authorization for tracking rate increases for purchased gas "did not extend to other cost elements, including transportation costs, such as are here sought by Panhandle." *Trunkline Gas Co.*, Docket No. CP78-43 (25 Sept. 1978), *reprinted in* J.A. at 136.

[77] Brief for Respondent at 45.

[78] *See* decisions cited *id.* at 44.

The Commission agrees that Account 489 "is the usual situs for revenues," but it claims that use of that account "would be inappropriate here" because Account 489 "defers revenues until a rate change proceeding under Section 4, and has no provision for flowing excess revenues back to Panhandle's jurisdictional customers." [79] Also conceding that nothing in the PGA regulations speak to transportation costs and revenues, the Commission argues that "nothing specifically precludes using these mechanisms to respond to the Commission's regulatory purposes." [80] It then cites authority that its powers must be construed broadly in the public interest.[81] It points out that in the absence of the condition, Panhandle would continue to "overcollect . . . the excess transportation revenues." [82]

We agree that " 'the Commission's broad responsibilities . . . demand a generous construction of its statutory authority,' " [83] but we do not believe the Commission should have authority to play fast and loose with its own regulations. It has become axiomatic that an agency is bound by its own regula-

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[79] *Id.* at 40.

[80] *Id.* at 41.

[81] *E.g., FPC* v. *Louisiana Power & Light Co.*, 406 U.S. 621 (1972).

[82] Brief for Respondent at 42 n.28.

[83] *FPC* v. *Louisiana Power & Light Co.*, 406 U.S. 621, 642 (1972) (quoting *Permian Basin Area Rate Cases*, 390 U.S. 747, 776 (1968)).

tions.[84] The fact that a regulation as written does not provide FERC a quick way to reach a desired result does not authorize it to ignore the regulation or label it "inappropriate." [85]

Thus, the order under review must be set aside because in requiring crediting of *transportation revenues* to the *purchased gas* account, the Commission violated its own regulations.[86]

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[84] *Service* v. *Dulles*, 354 U.S. 363 (1957); *Union of Concerned Scientists* v. *AEC*, 499 F.2d 1069, 1082 (D.C. Cir. 1974); *see United States* v. *Nixon*, 418 U.S. 683, 695-96 (1974); Note, *Violations by Agencies of Their Own Regulations* 87 HARV. L. REV. 629 (1974).

[85] Judge Wright suggests that the regulation's name "is inapt and the description incomplete," but because the regulation did not specifically forbid flow-through of transportation revenues, the "court should not mistake clumsy agency nomenclature for unlawful agency action." Concurring and Dissenting Opinion at 16. As we read the regulation and the order accompanying its promulgation, there was nothing clumsy or inapt about its name and description. The carefully constructed PGA provisions were meant only to pass on purchased gas cost adjustments; they were not meant to be a catchall through which the agency could make any interim adjustment it desired. While we generally should defer to agency interpretations of its own regulations, that is not appropriate here where the applicable regulations provide on their face that new transportation revenues belong in Account 489, not 191.

[86] Under authority of the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301-3432 (West Supp. 1979), the Commission recently issued new regulations requiring interstate pipelines to credit to Account 191 and thereby "flow back" to their customers revenues from transportation of natural gas for intrastate pipelines and local distribution companies to the extent such transportation revenues and volumes exceed representa-

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[79] *Id.* at 40.

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3. *The Condition Is Not Supported by Soundly Based Findings and Is Unreasonable*

Even assuming the revenue crediting provision did not violate Commission regulations and was within the ambit of the section 7(e) conditioning power, we find that the condition was not supported by soundly based findings in the record and was not reasonable.[87]

(a) *Basis for Revenue Crediting*

The Commission's theory for attaching the certificate condition is that (1) Panhandle's extant configuration of rates was designed to recover its full cost of service; (2) consequently, any uncontemplated revenues, such as those obtained through the transportation services in question, would permit double recovery of certain of Panhandle's items of cost and would *pro tanto* raise Panhandle's rate of

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tive levels used in determining cost of service and establishing rates. 44 Fed. Reg. 52185 (1979) (final rule amending 18 C.F.R. § 284.103). The Commission adopted the same rule respecting transportation agreements with certain end-users. 44 Fed. Reg. 30329-30 (1979) (to be codified at 18 C.F.R. § 284.205(b)). Since the enactment of the statute and promulgation of the regulations occurred after entry of the instant order, they provide no support for the Commission's decision here. The validity of the new regulations is not an issue in this case, and consequently we leave that question undecided.

[87] *See California Oil Co.* v. *FPC*, 315 F.2d 652, 656 (10th Cir. 1963); *Pure Oil Co.* v. *FPC*, 292 F.2d 350, 352-53 (7th Cir. 1961) (both cases hold that certificate conditions must be supported by soundly based findings in the record.

return, and consequently rates charged, above the just and reasonable level.[88] If the state of the world were as the Commission assumes it to be, the challenged condition may have in fact been reasonable. But, as Panhandle is at pains to emphasize throughout its brief, there is no reason to assume that existing revenues are adequate. The Commission's argument depends on the justness and reasonableness of the rates prescribed in Panhandle's 1975 ratemaking case.[89] Although the rates may have been just and reasonable in 1975 it is plain that they need not be so at present. If Panhandle's revenues do not presently recover the full cost of service, then the Commission's argument is substantively incorrect and works rather harshly.

It is not without significance that the Commission at no point made an express finding that Panhandle's rates continued to recover its full cost of service. The Commission merely assumed that they did. This seems to us a rather precarious assumption to make

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[88] Initially it appears that the Commission thought of the transportation services utilizing Panhandle's previously excess capacity as being costless and consequently required that the resulting revenues be fully credited against Account 191. The Commission on rehearing this case modified its initial position slightly, permitting the incremental costs associated with the transportation service to be offset against revenues prior to entry into Account 191. *See* note 9 and accompanying text *supra*.

[89] *Panhandle E. Pipe Line Co.*, Docket No. RP75-102 (the relevant order approving the settlement in part was issued 25 April 1977).

in view of the rising costs [90] in almost all aspects of society between the time the rate case was filed and the instant order entered. The validity of the assumption is also undermined by increases in need for and costs of transportation services, as evidenced in No. 78-1960. Further, as the Commission observed, the general rate level for Panhandle is presently the subject of another proceeding.[91]

We do not think that the Commission's dubious assumption as to the continuing adequacy of the 1975 rates qualifies as a "soundly based finding in the record" upon which section 7(e) conditions must be founded. In the absence of such support, the order must be set aside.[92]

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[90] The Commission acknowledged in *Natural Gas Pipeline Co. of America*, Docket No. CP78-439 (26 Dec. 1978), 5 F.E.R.C.—that pipeline utility costs have risen more than 36% since 1975 when Panhandle made its rate filing.

[91] Docket No. RP78-62.

[92] Our colleague argues that until Panhandle's rates "are revised, the Commission may operate as if they were still" adequate. He notes the language in *California Oil Co.* v. *FPC*, 315 F.2d 652, 655 (10th Cir. 1963), that § 7 proceedings are not "rate" cases involving "the complex and intricate problems as to what is a 'just and reasonable' price." Concurring and Dissenting Opinion at 17 n.24, 18 n.25. We agree that § 7 proceedings should not involve the question of what is a just and reasonable rate. But since the basis of the challenged order appears to be that increased transportation revenues will unduly raise Panhandle's rate of return—making its rates unjust and unreasonable—we think the Commission is obligated to find support for its assumptions in the record. In this case, we think the Commission's

(b) *Disallowing Offset of Revenues by New Transportation Costs Was Unreasonable*

Assuming arguendo that the Commission's order was authorized by section 7, did not violate its regulations, and was otherwise supported by soundly based findings in the record, we think the order was unreasonable because it did not allow offset of revenues by increased transportation costs. In its application for reconsideration and rehearing to FERC in the LOF proceeding, Panhandle urged that requiring crediting of revenues and prohibiting flow-through of increased transportation costs constituted a double penalty. The company expressed a willingness to develop with the Commission staff "an appropriate provision dealing with the flow-through of transportation costs paid by Panhandle to others as well as transportation revenues received by Panhandle from

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reference to the prior, and possibly outdated, rate case is inadequate support for the condition.

Judge Wright also suggests that "Panhandle has no more right to *increase* its rate of return by keeping new transportation revenues—without resorting to Section 4—than FERC has to *decrease* the rate of return using its Section 7 powers." *Id.* at 16-17. We disagree. As we read the Act, if a pipeline desires to earn more money by providing a new service, it need simply apply for a § 7 certificate. Nowhere do we find a requirement that the pipeline also initiate a § 4 proceeding to be able to retain such revenues. If the Commission fears that such new services will drive the pipeline's rate of return above the just and reasonable level, it may resort to a § 5 proceeding, or utilize other possible remedies we outlined at notes 66-68 and accompanying text *supra*.

others." [93] The Commission's response was that Panhandle was free at any time to submit a section 4 general rate change in the event its other transportation costs were preventing it from earning a reasonable return.[94]

Panhandle argues that the Commission's "facile response . . . fall[s] woefully shy of the 'reasoned consideration' standard that is required by law." [95] FERC maintains its disposition was correct because the revenue crediting requirement was "directly connected" to the Commission's section 7 conditioning power, but the request to flow through costs for "unspecified transportation services" was "more suited to a general rate case where a general tracking provision might be allowed." [96]

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[93] Application for Reconsideration and Rehearing, *reprinted in* J.A. at 65-66.

[94] *Panhandle E. Pipe Line Co.*, Docket No. CP77-479 (22 Feb. 1978), *reprinted in* J.A. at 69.

[95] Brief of Petitioner at 36.

[96] Brief for Respondent at 31. The Commission also argues that to the extent Panhandle's request sought "to pass on additional charges to its customers," § 4 would require a full cost-of-service showing. *Id.* However, we think that if the Commission had power under § 7 to adjust rates downward without a § 5 proceeding (as we here assume arguendo), it would similarly have authority under § 7 to allow rates to rise without a § 4 proceeding. And even if § 4 somehow prevented flow-through of net transportation cost increases, the Commission at least should have allowed the new revenues to be offset by new costs to the extent costs did not exceed revenues, since no net increases in costs would thereby result.

We find the Commission's justifications inadequate. The fact that Panhandle could seek a tracking provision in a rate case does not make inappropriate the allowance of an offset of transportation costs against transportation revenues before crediting the balance for resale customers. Furthermore, we think such a netting procedure would be essential where both transportation costs and revenues were unanticipated —even assuming the pipeline was in other respects recovering its costs. The unforeseen income may increase a pipeline's revenues above the just and reasonable level, but the unforeseen costs, at the same time, would directly reduce the size of this "overcollection." If any amount needed to be credited under the Commission's theory, we think it would be the unanticipated revenues from transportation for others less the unanticipated costs of transportation by other pipelines.

Therefore, we think the Commission's order was unreasonable to the extent it did not allow netting out of new transportation costs prior to the entry of the credit in Account 191.[97]

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[97] In his opinion concurring in part and dissenting in part, Chief Judge Wright agrees with us that the Commission acted unreasonably in treating transportation costs and revenues differently. However, he also claims that our holding the Commission's action unreasonable as an additional ground for reversal gives rise to the anomaly of "alternative holdings" leading to "different results." Concurring and Dissenting Opinion at 10 n.19. This is not the case. We do not mean to imply that the invalidity of the instant order would be remedied merely by an infusion of evenhanded treatment of revenues and costs. On remand, under our decision, not

4. *Conclusion—No. 78-1356*

Because the order under review in No. 1356 constituted an improper exercise of the Commission's section 7 conditioning power, violated the Commission's accounting regulations, was not supported by soundly based findings in the record, and was unreasonable in the absence of an offset, we set it aside, and remand the case for further proceedings not inconsistent with this opinion.

B. *No. 78-1960*

The order under review in No. 78-1960 involved the Commission's disposition of a Panhandle filing "prepared in an effort to find an acceptable solution to the serious problems" flowing from FERC's revenue crediting policy.[98] Panhandle's proposal was to include additional transportation costs and charges in Account 191 in the same way it was compelled to credit its transportation revenues. The Commission rejected the suggestion. Because we today invalidate the revenue crediting policy, in large measure the questions raised in this petition resolve themselves. To the extent issues in this petition are not mooted by our disposition of No. 78-1356, we affirm the Commission's order.

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only must the Commission's orders stay within the bounds of reasonableness, but also within parameters supported by sufficient findings with record support, its statutory authority, and its regulations.

[98] Supplemental Brief of Petitioner at 6.

Panhandle argues that the Commission's refusal to allow the pipeline "to recover, as an offset to Account No. 191," new transportation costs was based upon "bald, wholly unsupported assumptions as to the adequacy of Panhandle's overall rate level," and therefore violated section 5.[99] If Panhandle is referring to the Commission's refusal to net out transportation costs from revenues before crediting, there may be some validity to the argument.[100] That question is mooted, however, since we void the revenue crediting procedure in No. 78-1356. If, on the other hand, Panhandle is arguing that prohibiting flow-through of transportation costs is violative of section 5 even in the absence of revenue crediting, we cannot agree. Refusal to allow flow-through of increased costs does not constitute a rate change, and therefore the policies of section 5 simply do not apply.

Panhandle also contends that the Commission has confused the provisions of sections 4 and 5, by "thrust[ing] upon Panhandle an unlawful requirement that it forfeit its new transportation revenues automatically, and in addition be obliged to commence Section 4 general rate case proceedings to restore the funds needed to meet its expenses for transportation for others."[101] Again, in view of today's holding, this issue is moot.

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[99] *Id.* at 9.

[100] Indeed, elsewhere in today's opinion we hold it unreasonable to disallow an appropriate offset before crediting.

[101] Supplemental Brief of Petitioner at 14.

The pipeline submits that it is error for the Commission to interpret the PGA regulations to include transportation revenues but not costs. It argues, "The Commission cannot have it both ways. Either its regulations permit including transportation items in the purchased gas accounts or they do not. Panhandle submits that they do not . . . ." [102] We agree with Panhandle. But since the PGA regulations do not permit inclusion of transportation items, the Commission's refusal to allow transportation costs to flow through Account 191 must be upheld.

Panhandle's final argument is that it is arbitrary and contrary to precedent to disallow pass-through of increased transportation costs. It argues that since the Commission's assumption regarding Panhandle's PGA clause is that the pipeline "cannot absorb additional gas purchase expenses, and must recover such costs through the PGA clause, it is not permissible for the Commission to assume at the same time that the related transportation costs can be absorbed —at least without some examination of the cost of service and Panhandle's revenue requirements." [103] If Panhandle is arguing that refusal to allow transportation cost recovery is arbitrary in the context of the revenue crediting requirement, the argument is moot. If it is suggesting that it is absolutely entitled to pass on transportation costs in the absence of an affirmative finding by the Commission that the

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[102] *Id.* at 18.

[103] *Id.* at 19.

pipeline can absorb the increased costs, we disagree. It probably would be wise for the Commission to adopt a mechanism in appropriate proceedings allowing transportation costs similar treatment to that of purchased gas costs, but we do not think it arbitrary for the Commission to refuse to expand the definition of purchased gas costs to benefit Panhandle in a section 7 certificate proceeding for Trunkline. We think the decision to construe narrowly the PGA regulation falls within that zone of reasonableness immunizing it from reversal.

Panhandle points out that in *Tennessee Gas Pipeline Co.*[104] and *Texas Eastern Transmission Corp.*[105] the Commission allowed tracking of transportation charges. These cases involved special storage arrangements, and the Commission was careful in each one to deny precedential value to the cases. The holdings have not been followed in subsequent cases, and FERC submits that *Tennessee Gas* and *Texas Eastern* "are anomalies in a sea of consistent Commission rulings rejecting rate filings of this nature."[106] It is not denied that the Commission has a policy against permitting tracking of transportation charges outside of settlement agreements. That the Commission granted two *sui generis* exceptions when special storage arrangements were involved certainly does

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[104] Docket No. CP77-419 (10 Nov. 1977).

[105] Docket No. CP77-313 (27 Jan. 1978).

[106] Brief for Respondent at 52.

not compel it to allow tracking when more general transportation situations arise.[107]

Therefore, we conclude that the order in No. 78-1960 must be affirmed to the extent that the issues therein are not mooted by our disposition of No. 78-1356.

C. *No. 78-1630*

The orders reviewed in No. 78-1630 are related to those in Nos. 78-1356 and 1960 in that they involve rates charged and costs incurred by Panhandle for natural gas transportation services. The pipeline argues that it was arbitrary for the Commission to waive its requirements of a full cost-of-service showing to allow a rate decrease, but refuse to do so as to a related cost increase.[108] The Commission responds that its primary duty is to protect the interest of consumers, and therefore waiving requirements to allow rate decreases, but not increases, was within the breadth of its discretion. FERC concedes that

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[107] Similarly, we do not believe the narrow holding in *Richmond Power & Light* v. *FERC*, 574 F.2d 610 (D.C. Cir. 1978) requires the Commission to allow Panhandle to track transportation cost increases. In *Richmond*, this court held merely that the Commission had "reached an informed and reasoned decision" in permitting transmitters of electricity in the "coal by wire" program to include fixed costs in their special short term services without having to credit the transmission revenues. *Id.* at 620-22. The decision may cast a shadow on the Commission's revenue crediting procedure in No. 78-1356, but it does not mandate adoption of a general transportation tracking provision by FERC.

[108] Brief of Petitioner at 26, 48-52.

Panhandle "has now set forth in its brief . . . some data which may be sufficient to call for a reexamination of the denial of waiver" but argues that the company "has not submitted that data to the Commission as required by the Natural Gas Act." The Commission suggests that "[i]f Panhandle believes that it has sufficient cause to be granted a waiver, then it should request the Commission to grant such a waiver in the first instance." [109]

We think Panhandle's application for rehearing made it sufficiently clear that it was seeking a waiver of pertinent regulations. Furthermore, we believe the Commission had the relevant data before it to rule on the request.

Although we agree with the Commission that accepting rate decreases generally does not compel it to accept related rate increases, we think that on the facts of the disputed order, it was an abuse of discretion not to allow Panhandle to pass on its costs. Due to the location of delivery points, it appears that Panhandle makes no charge to Northern for its services. In seeking the rate increase, Panhandle was merely attempting to pass on dollar for dollar rate increases approved by the Commission for upstream pipelines. The Commission has authority to waive requirements of tracking authority in a proper case. We think that where a pipeline is merely an accounting conduit for charges made by other pipelines, good cause exists to grant a waiver.

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[109] Brief for Respondent at 53-55.

For these reasons, we set aside that portion of the Commission's order denying Panhandle's rate increase in FERC Docket No. RP78-39, and remand the case for further proceedings consistent with this opinion. Since it appears that Panhandle does not object to the Commission's acceptance of the pipeline's rate decrease in FERC Docket No. RP78-40—except to the extent that it demonstrates discriminatory treatment—that portion of the order is affirmed.[110]

III. CONCLUSION

In sum, we find that the Commission's rather novel revenue crediting procedure must be disapproved in this context because it is not authorized by section 7(e), it is violative of the Commission's accounting regulations, it is not supported by soundly based findings in the record and it is unreasonable. We therefore vacate the order in No. 78-1356 and remand the case for further proceedings consistent with this

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[110] Judge Wright suggests that by approving Commission waivers of tracking and cost-of-service-hearing requirements we "silently admit[] that alterations in rates may be made outside of § 4 and § 5 proceedings." Concurring and Dissenting Opinion at 10 n.19. This, he argues, is inconsistent with our holding in No. 78-1356 that § 7 does not authorize adjustment of rates for services not before the Commission in the relevant certificate proceeding. We do not think the dispositions inconsistent. No. 78-1356 involves the Commission's attempt *under § 7* to adjust rates for services not before it; No. 78-1630 involves the propriety of the Commission's exercise of its *uncontested power to waive the cost-of-service-showing requirement in accepting new rate filings*, absent tracking authority.

opinion. Because we invalidate the revenue crediting approach in No. 78-1356, we find the issues in No. 78-1960 largely mooted; to the extent they are not, we affirm the Commission's disposition. Finally, we vacate that portion of the order in No. 78-1630 prohibiting Panhandle to pass on its increased costs, affirm that portion approving Panhandle's filing of decreased rates, and remand the case for further proceedings consistent with this opinion.

WRIGHT, *Chief Judge, concurring in part and dissenting in part*: Panhandle Eastern Pipeline Company (Panhandle) challenges certain orders of the Federal Energy Regulatory Commission (FERC) relating to costs and revenues associated with the transportation of natural gas.[1] The first order, in No. 78-1356,[2] requires that Panhandle flow through[3] to its resale gas customers the revenue it will gain from transporting natural gas for another company by crediting that revenue to its "purchased gas ac-

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[1] The petitions for review were filed pursuant to § 19(b) of the Natural Gas Act, 15 U.S.C. § 717r (1976).

[2] *Panhandle Eastern Pipe Line Co.*, Docket No. CP77-479 (Dec. 16, 1977), *reprinted in* Joint Appendix (JA) at 50-62, *modified* (Feb. 22, 1978), *reprinted in* JA 68-71.

[3] The awkward term "to flow through" is used to denote an accounting method that permits a particular item of cost or revenue to be charged or credited to a company's customers directly; the procedure is in contrast to the usual ratemaking procedure, in which changes in cost or revenue merely affect the setting of the prospective rate after the next ratemaking proceeding.

count." The second, in No. 78-1960,[4] denies Panhandle the right to flow through the cost of obtaining transportation services from other pipelines. The remaining orders, in No. 78-1630,[5] require Panhandle to absorb increased costs but allow it to flow through savings from decreased charges associated with certain transportation contracts. In these contracts Panhandle serves as a mere accounting conduit between other pipelines. The majority vacates the first order, affirms the second, vacates the portion of the third requiring Panhandle absorb increased costs, and affirms the remainder of a third.

I join in the majority's disposition of the third order. As indicated in the majority opinion, in neither the order nor its brief does FERC provide any real justification for its decision to waive the requirement of tracking authority for rate decreases, but not for rate increases. Indeed, it seems to me that the Government admits to justice of Panhandle's claim when it says:

> Although [Panhandle] has now set forth in its brief here some data which may be sufficient to call for a reexamination of the denial of a waiver, it has not submitted that data to the Commission as required by the Natural Gas

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[4] *Trunkline Gas Co.*, Docket No. CP78-43 (April 17, 1978), *reprinted in* JA 119-126, *rehearing denied* (Sept. 25, 1978), *reprinted in* JA 135-139.

[5] *Panhandle Eastern Pipe Line Co.*, Docket Nos. RP78-39 and RP78-40 (March 10, 1978), *reprinted in* JA 91-92, *rehearing denied* (May 9, 1978), *reprinted in* JA 99-103. These orders will be referred to collectively as "the third order."

> Act. * * * If Panhandle believes that it has sufficient cause to be granted a waiver then it should request the Commission to grant such a waiver in the first instance. * * *

Brief for respondent at 54-55 (citations omitted). According to the working papers, Panhandle *did* present to FERC at the time of its requested waiver all the data it now presents to this court. I therefore consider it appropriate to grant Panhandle relief from the onerous decision of the Commission without further procedure complication. In joining the majority on this point, however, I would emphasize that my agreement is limited to cases in which the pipeline involved is merely an accounting conduit.[6] Where the pipeline actually makes a charge for providing transportation services, I believe a different case would be presented.

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[6] Panhandle's "accounting conduit" status arises from arrangements between it and four other pipelines. An explanation of one of the deals will suffice. In it, Panhandle delivers gas to Northern Natural Gas Company at a point of intersection between the two pipelines. Panhandle in turn receives gas from Trunkline Gas Company (and indirectly from two other pipeline companies as well) at a point of intersection *downstream from* the first point. Thus the entire fee charged by Panhandle to Northern is remitted to Trunkline; no part of the cost of transportation is attributable to Panhandle's operations. *See* brief for petitioner at 49-50. FERC's decision in Docket No. RP78-11 (Dec. 1, 1977) to increase the transportation fees payable to Trunkline, coupled with its refusal in the order now under review to permit Panhandle to increase the fees payable by Northern, thus constitutes an inexplicable penalty imposed on Panhandle in favor of Northern.

In the remainder of this opinion I shall discuss only the first two orders.[7]

I

A

The orders under review represent an attempt by FERC to accommodate the changing economics of natural gas pipeline operation to the provisions of the Natural Gas Act of 1938, 52 STAT. 821, 15 U.S.C. §§ 717-717z (1976 & Supp. I 1977) (as amended). It is therefore necessary to review briefly the features of the Act and the general problem faced by the Commission in its application today.

We are primarily concerned with three sections of the Act, Sections 4, 5, and 7. Section 7, 15 U.S.C. § 717f, is the provision for initial rate review. It requires all "natural gas companies," a term which encompasses interstate natural gas pipelines,[8] to obtain a "certificate of public convenience and necessity" from the Commission before offering new services. This certificate may be granted subject to "such reasonable terms and conditions as the public convenience and necessity may require." Section 7 (e), 15 U.S.C. § 717f(e). FERC will commonly condition the certificate upon a rate lower than the contract rate,[9] or upon a contingent refund obliga-

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[7] *See also* note 19 *infra.*

[8] 15 U.S.C. § 717a(b) (1976).

[9] *See Atlantic Refining Co.* v. *Public Service Comm'n*, 360 U.S. 378 (1959).

tion.[10] Temporary certificates may be issued in emergencies without notice or hearing pursuant to Section 7(c); permanent certificates, issued pursuant to Section 7(e), require notice and hearing unless the parties waive their right to a hearing.

Once rates for a pipeline are set, they may be changed at the instigation of the pipeline company or the Commission.[11] The pipeline company may obtain a rate increase by filing a new rate schedule 30 days in advance of its taking effect, pursuant to Section 4, 15 U.S.C. § 717c. The Commission, by acting within the 30 days, may suspend the new rates for a five-month period. If a hearing on the new rates is not completed within the five months, the new rates may be put into effect, subject to the obligation of the pipeline company to refund the excess if the Commission subsequently determines the rates to be above the just and reasonable rate. The burden is on the company to prove the justice and reasonableness of the new rates. Section 4(d)-(e).

If at any time the Commission suspects that the current rates charged by a pipeline company are above the just and reasonable level, it may order a hearing pursuant to Section 5, 15 U.S.C. § 717d. After the hearing the Commission may determine

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[10] *See FPC* v. *Sunray DX Oil Co.*, 391 U.S. 9 (1968).

[11] Other affected parties may instigate a rate change by petitioning the Commission. 15 U.S.C. § 717d (1976).

the just and reasonable rate and order the company to conform to it.[12]

Rapid changes in natural gas costs occurring over short periods of time—resulting primarily from the much-lamented "energy crisis"—have induced the Commission to make adaptations in the statutory procedures. The primary instance of such adaptation concerns the treatment of changes in the cost of natural gas itself. As explained in Order No. 452, 47 FPC 1049 (1972), *modified*, Order No. 452-A, 47 FPC 1510 (1972), *amended*, Order No. 452-B, 49 FPC 84 (1973), the Commission recognizes that the cost of purchased gas is, for most natural gas companies, the largest single component of their cost of service. In a time of rising gas costs, pipeline companies seek a form of "tracking" provision which enables them to flow through the increased gas cost to their customers automatically. If unable to obtain "tracking" authority, pipeline companies must file frequent rate increases pursuant to Section 4. Such increased filings are burdensome to both the Commission and the companies. They produce a backlog of rate filings for FERC to review, thus prolonging and delaying the administrative process. Moreover, the contingent refund obligations of natural gas companies pursuant to Section 4(e) swell, and may lead to extensive and unpredictable shifts in natural gas rates charged to consumers.

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[12] FERC has no authority under § 5 to *increase* the company's rates, unless the company has filed a new rate schedule. 15 U.S.C. § 717d (1976).

Responding to this problem, FERC adopted a procedure called a "purchased gas cost adjustment provision." *Id.*; *see* 18 C.F.R. § 154.38(d)(4) (1979). The essential purpose of the provision is to obviate the need for natural gas companies to resort to cumbersome Section 4 proceedings. It permits them to alter their rates in response to changes in the cost of their purchased gas, without full reexamination of cost-of-service data. In effect the rate is adjusted in response to changes in one variable—the cost of purchased gas—with all other components of cost-of-service assumed to remain constant.

The mechanism for this adjustment is called the "unrecovered purchased gas cost account," numbered Account 191, *see* 18 C.F.R. Part 201 (1979). Increases or decreases in purchased gas costs are registered in the account. Every six months the company's rates are adjusted, so that over the next six-month period the revenue shortfall or excess will be amortized to zero. Thus, if the purchased gas costs of the company increases, the amount of that increase will be recorded in Account 191; at the end of the six-month period the rates will be surcharged an amount sufficient to restore the company's net revenues to the level prevailing before the cost increase. Conversely, if the purchased gas costs declines, then natural gas consumers will receive a compensating decrease in their rates during the succeeding six-month period. These changes require no examination of the underlying cost-of-service of the company. The public is protected, however, by the requirement that

cost decreases as well as increases be reflected in the purchased gas account, and by periodic (every 36 months) review by the Commission of the company's total cost of service and the effect of the purchased gas account.

The natural gas industry has recently undergone another change in conditions that again may require an adaptation of FERC's procedures. As a result of the natural gas shortages starting in the first part of the 1970's, many natural gas pipelines have had to obtain new sources of gas, often not connected to their established pipelines. Accordingly, it has become common for one natural gas company to transport gas for another from the gas producer to the other company's established pipeline. Generally, this sort of arrangement entails little additional cost to the transporting company, because the shortage has left excess capacity in the pipelines. Accordingly, the costs and revenues of pipeline companies may fluctuate widely. If transporting for others, the pipeline company receives a large amount of revenue, with little attendant incremental cost. If purchasing transportation services from others, it incurs great unanticipated cost.

The orders under review reflect FERC's initial attempt to solve the problem of these cost and revenue fluctuations. As in the case of the purchased gas cost problem, the solution may be to obviate resort to the procedures of Sections 4 and 5, lest backlogs, administrative delays, and contingent liabilities proliferate. It is not for this court to de-

cide precisely how FERC should respond to the problem of new transportation costs and revenues;[13] we must, however, decide whether the Commission has the statutory authority to respond as it did, and whether that response is reasonable and fair. I therefore turn my attention to the orders under review.

B

The first order concerns the treatment of revenues received by Panhandle from an agreement to transport up to 1,800 Mcf of natural gas on a firm basis and 1,200 Mcf on a best efforts basis for eventual delivery to an industrial consumer, Libby-Owens-Ford Company. Panhandle is to be paid $7,650 per month for its services.[14] Since Panhandle will be able to provide this transportation without substantial additional cost, because of its excess capacity, Panhandle will receive nearly $7,650 monthly in additional net revenues. FERC agreed to this arrange-

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[13] No one can doubt that FERC has the power to adopt procedures it deems most efficient in effectuating the purposes of the Act. As the Supreme Court has emphasized, the Act does not prescribe a "rate-changing 'procedure,' " *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332, 342 (1956). Rather, the Act "defin[es] and implement[s] the powers of the Commission to review rates set initially by natural gas companies * * *." *Id.* at 343. So long as FERC performs its responsibility to review rates searchingly in the public interest, within the authority delegated by the Act, and in accordance with its own regulations and precedent, this court should not dictate a particular form or procedure.

[14] This rate was approved by FERC, *Panhandle Eastern Pipe Line Co.*, Docket No. CP77-479 (Dec. 16, 1977), *reprinted in* JA 50-62.

ment, subject to the condition that this increase in net revenues be flowed through to the resale gas customers, by crediting the additional net revenue to Panhandle's purchased gas account. In that way the revenues could be accumulated during each six-month period, and flowed through during the next, without any party being required to resort to the cumbersome procedures for rate changes set up in Sections 4 and 5 of the Act.

The majority declares this procedure illegitimate, suspecting it of being an under-the-cover way for FERC to lower the just and reasonable rates established in a full Section 4 ratemaking proceeding. I, however, cannot view this procedure as altering in any way the results of that earlier proceeding. All the Commission has attempted to do is to govern the use of revenues generated from a new service. As I will explain in more detail below,[15] I believe the Commission's Section 7 power to condition a certificate of public convenience and necessity is ample to support an order of this kind.

The second order concerns the treatment of transportation charges incurred by Panhandle in connection with a new agreement between Panhandle and three other pipelines. Panhandle pays the others an estimated $1.5 to $2 million per year to transport natural gas from off-shore Louisiana to Panhadle's line in the Midwest; the company therefore petitioned FERC for permission to include the new transportation costs in the purchased gas account, which would

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[15] *See* Part III *infra*.

enable it to flow the newly-incurred costs directly through to its customers. FERC denied this petition, in effect ruling that Panhandle must absorb the increased cost until such time as its rates are revised in a Section 4 proceeding.

Panhandle contends that this treatment of new transportation costs is inconsistent with FERC's treatment of new transportation revenues in the first order. The majority apparently agrees with this contention, but finds it unnecessary to reverse the second order because the inconsistency is removed by the reversal of the first order. The majority concludes:

> It probably would be wise for the Commission to adopt a mechanism in appropriate proceedings allowing transportation costs similar treatment to that of purchased gas costs, but we do not think it arbitrary for the Commission to refuse to expand the definition of purchased gas costs to benefit Panhandle in a section 7 certificate proceeding for Trunkline. * * *

Majority opinion, —— F.2d —— (p. 40). I agree with this conclusion insofar as it recognizes the Commission's authority to adopt whatever reasonable procedures it deems necessary to deal with new transportation costs. I am disturbed, however, at the cumulative effect of the majority's treatment of the two orders.

In my view, the Commission is fully within its powers when it seeks to provide an expeditious procedure for accounting for changes in various costs

and revenues that occur between Section 4 proceedings. Neither the first nor the second order is, in itself, arbitrary, unreasonable, or in excess of the Commission's delegated power. The majority, however, would prevent the Commission in the first order from adopting an expeditious procedure for dealing with increased revenues. In the second order the majority would permit the Commission to refrain from adopting such a procedure for dealing with increased costs. By the combination of the two positions, the majority effectively prevents the Commission from adopting expeditious procedures altogether. Even though the opinion purports in dictum to endorse "tracking" [16] or, in the alternative, allowing a "cross-refund" of excess profits as determined in a later proceeding,[17] I believe its holding—that the Commission lacks statutory authority to condition Section 7 certificates on a revenue flow-through to customers—will preclude any such procedures in this case.[18] The result of the majority's approach will be

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[16] *See* majority op., text and notes at notes 66-68.

[17] *See id.* at note 68.

[18] Because we are dealing with new, previously uncertificated transportation services, it is not likely that a general transportation "tracker" adopted at a previous § 4 proceeding would be applicable on its terms to the new service. The majority implies that if a pipeline company has the foresight and foreknowledge to request and receive a transportation "tracker" that would apply to new transportation services when they are certificated, such a "tracker" would be lawful. In this I agree. But in my view a § 7 proceeding is a more logical and appropriate occasion to decide on the treatment of costs and revenues associated with a *new* service. I do not

to force both the Commission and the pipelines to employ the Section 4 and Section 5 procedures more frequently, even though a separate treatment of new transportation costs and revenues is legitimate and practical. This, in my judgment, is contrary to the interest of both Commission and pipeline; more important, it is contrary to the public's overriding interest in the efficient setting of just and reasonable rates.[19]

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see why the lack of tracking authority for previously certificated services prevents adoption of such authority for a new service.

[19] As I understand its opinion, the majority does not disagree with this statement of the usefulness of expeditious procedures to accommodate cost and revenue fluctuations between § 4 proceedings. We disagree primarily on the issue of the scope of FERC's statutory authority to make the necessary accommodations. The majority's restrictive view, however, has produced several inconsistencies.

First, the majority appears to endorse the "purchased gas cost adjustment provision" of 18 C.F.R. § 154.38(d)(4)(1978). *See* majority op., text and notes at notes 69-86. Yet this provision serves to increase rates without a § 4 proceeding, or to decrease rates without a § 5 proceeding; thus it would seem to be impermissible under the majority's analysis. Admittedly, a purchased gas adjustment clause is established pursuant to a § 4 proceeding, but the majority does not explain where the Commission derives its authority to alter the statutory scheme—as the majority sees it—in the course of a § 4 proceeding, any more than it may do so in a § 7 proceeding.

Second, the majority says that "the order was unreasonable because it did not allow offset of revenues by increased transportation costs." Majority op., —— F.2d at —— (p. 36). The majority suggests that such a "netting procedure" could be "essential." *Id.*, —— F.2d at —— (p. 37). Yet, if new revenues exceed new costs, then the rates would be lowered

Nevertheless, as I explain in more detail below, *see* Part III *infra*, I agree that FERC has acted unreasonably in its inconsistent treatment of new transportation costs and revenues. I do not believe that FERC has suggested any acceptable explanation—in terms either of procedural differences between the two or of substantive differences—that justifies this inconsistency. I reach this conclusion not out of solicitude for the fortunes of Panhandle's shareholders, but out of a conviction that consumers in the long run will be better off when rules are adopted

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without resort to § 5, and without any "tracking" provision. Again, this violates the principle enunciated by the majority in its Part II-A-1. Apparently the majority intended to propound alternative holdings. If so, there ensues the anomaly that the two alternative *holdings* lead to different *results*: under one, no revenue crediting is permitted at all, while under the other, such crediting is permitted subject to a cost offset.

Finally, the majority's disposition of the third order, *see id.*, —— F.2d at —— (pp. 41-43), conflicts with the analysis of the first order. In the third order the majority permits FERC to alter rates without a cost-of-service proceeding, in the absence of tracking authority. By affirming the Commission's decision to waive tracking authority in the third order, the majority silently admits that alterations in rates may be made outside of § 4 or § 5 proceedings.

I believe the majority's endorsement—implied or otherwise—of the purchased gas adjustment provisions, offset of new transportation revenues by costs, and waiver of tracking authority is commendable. But I suggest that, since the majority's restrictive interpretation of the Commission's powers is inconsistent with these and other sensible procedures, that interpretation—which in my view is a misreading of the Natural Gas Act—should be rejected. As it is, the majority's view is so pocked with exceptions as to be incomprehensible.

that will lead to effective setting of just and reasonable rates. Any procedure that induces a regulated party to turn to complicated and costly procedures when simple and inexpensive ones will do and any procedure that induces regulated parties to avoid transactions beneficial to the public because of unreasonable treatment at the hands of the Commission, will ill serve the public interest.

I would therefore hold that the orders in Nos. 78-1356 and 78-1960 be vacated and remanded to the Commission to give the Commission the opportunity to select, in the light of its experience and expertise, a fair and expeditious procedure for accounting for new transportation costs and revenues. I believe the Commission, and not this court, is in the best position to make this judgment. On remand, however, the Commission must bear in mind its obligation to deal evenhandedly with the parties; accordingly, the Commission must devise a method for treating parallel costs and revenues in the same manner, so far as possible.

II

A

The majority rightly recognizes that the "actual language of Section 7(e) is broad indeed," majority opinion, —— F.2d at —— (p. 17), but it contends that the Section 7 power falls short of that required to order a revenue flow-through in the first order under review. The majority reaches this conclusion primarily because of a mischaracterization of the FERC order. The majority treats the order as if

it were one "adjusting previously approved rates for services not before the Commission in the relevant certificate proceeding." *Id.* This it is not. *Rates* are not adjusted; only the size of future rate changes via the purchased gas account is affected. The Commission has not reevaluated Panhandle's cost of service, nor has it, as the majority implies, used the Section 7 conditioning power as a vehicle for lowering Panhandle's otherwise applicable rate of return. *All* that the first order accomplishes is to require Panhandle to dispose of *new* revenues in a particular way—*i.e.*, to flow those revenues through to its resale customers. Admittedly, those customers are better off than before the order. Panhandle, however, is *neither better off nor worse off* than before. The effect of the order is to leave Panhandle's rate of return at exactly the same level as before the order.

This is the classic situation in which the Commission employs the Section 7 conditioning power—to "hold the line," or maintain the *status quo*—until a full cost-of-service proceeding is completed.[20] If FERC were to condition a new service upon an overall lowering of the rate of return, I might have to agree that it had overstepped its authority. That is not this case.[21]

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[20] *See Atlantic Refining Co.* v. *Public Service Comm'n*, *supra* note 9, 360 U.S. at 392.

[21] Strictly speaking, this case does not even involve a lowering of rates. The revenue flow-through requirement will merely reduce the size of the purchased gas account surcharge in the next period. So long as new transportation revenues

Once the majority's mischaracterization of the order is corrected, its three arguments that the Commission exceeded its Section 7 authority are quickly disposed of. First, the majority argues that the procedure adopted by FERC in this order would "emasculate the role of Section 5 in the ratemaking scheme," *id.*, —— F.2d at —— (p. 17), by enabling FERC to lower a pipeline company's rates by attaching conditions to new certificates. Second, it argues that the procedure erodes the protections against "regulatory lag" and "rate instability," *id.*, —— F.2d at —— (p. 18), by exposing pipeline companies to unexpected rate reductions. Third, it argues that the procedure circumvents the Section 5 requirements of a hearing and findings of justness and reasonableness of rates, *id.*, —— F.2d at —— (p. 20).

These three are merely restatements of the one argument—that the Commission used its Section 7 power to lower the rates on Panhandle's other services. The answer is the same: the underlying cost-of-service and rate-of-return determinations are unchanged by the order; only the disposition of *new* revenues is affected. Unless the majority seeks to prevent *all* rate adjustments between Section 4 or Section 5 proceedings, including tracking clauses, purchased gas adjustment clauses, and the like, there is no reason to deny FERC the authority to maintain

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minus new transportation costs are smaller than the increase in gas costs, the rates to the consumer will continue to increase.

the *status quo* by flowing new revenues through to the pipeline customers.

Most of the precedent concerning the scope of the Section 7 conditioning power concerns the setting of rates or contract terms for the certified service, as the majority observes. *See* majority opinion, text and note at note 60. But there is no hint in those cases that the conditioning power is *limited* to the setting rates for certificated services. Indeed, such a holding is precluded by the very language of the Act: "The Commission shall have the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require." Section 7(e), 15 U.S.C. § 717 f(e) (1976). The order requiring Panhandle to flow its new transportation revenues through to its customers falls squarely within the apparent meaning of the statutory language. The burden is on the majority to show why the order exceeded that language; the fact that previous cases have concerned a different type of condition avails little.

The majority assumes that the revenue flow-through requirement here imposed would have been permissible pursuant to a Section 4 proceeding, but that for some reason it could not be imposed in a Section 7 proceeding. *See* majority opinion, —— F.2d at —— (pp. 27-28). This misconceives the differences between the two sections. Section 4 has no magical property that affords the Commission greater powers than it otherwise would have. Rather, the main difference between the sections is that Sec-

tion 4 is the mechanism for evaluating changes in the costs associated with already-certificated services, while Section 7 provides the mechanism for pricing and conditioning new services. Under Section 7 FERC has ample authority to ensure that certification of a new service—such as transportation—does not create an imbalance in the pipeline company's overall profit structure.

B

The majority also accepts Panhandle's argument that the first order under review violates the Commission's regulations. This argument is based on the name and description of Account 191, the account for "unrecovered purchased gas costs." This account has been described above;[22] needless to say, the majority is correct when it concludes that the name and description of the account refer to "*costs*, not *revenues*, and to *purchased gas* items, not *transportation* items." Majority opinion, —— F.2d at —— (p. 31) (emphasis in original). There is no question but that the original purpose of the account was to accommodate changes in the cost of purchased gas. The existence of Account 489, entitled "Revenues from Transportation of Gas for Others," bolsters the majority's argument. The implication is that new transportation revenues belong in Account 489, not Account 191.

Admittedly, the name of the account is inapt and the description incomplete; but this does not con-

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[22] *See* text and notes at notes 12-13 *supra*.

stitute a violation of the regulations. The fact that certain items are required by regulation to be included in Account 191 does not imply that the Commission may not also use that account for other items. There is no FERC regulation that *forbids* the practice adopted by the Commission in this order. Indeed, in decisions promulgated after the order under review here(and consequently no direct support for the Commission's position in this case), FERC adopted new regulations requiring the crediting of new transportation revenues to Account 191. 44 FED. REG. 52185 (1979) (amending 18 C.F.R. § 284.103); *id.* at 30329-30330 (amending 18 C.F.R. § 284.205(b)).

Looking behind the names on the accounts reveals that Account 191 is more appropriate than Account 489 in these circumstances: the latter is an ordinary revenue account, which does not provide for flowing through revenue, while Account 191 is precisely designed to serve the purposes of accommodating changes in costs and revenues on a six-month basis. Perhaps the names and descriptions of the accounts should be changed, but this court should not mistake clumsy agency nomenclature for unlawful agency action.

C

The majority also sets aside the Commission's first order because it was not based on "an express finding that Panhandle's rates continued to recover its full cost of service." Majority opinion, —— F.2d at —— (p. 34). According to the majority, such an express

finding is necessary before the Commission might order the new transportation revenues to be flowed through to Panhandle's customers, because otherwise the company might be deprived of a just and reasonable rate of return. The majority misconceives the nature of the Commission's assumptions.

In deciding to require the revenue flow-through, FERC did not, impliedly or otherwise, determine that Panhandle's revenues are still adequate to meet its cost of service, which was last determined in 1975.[23] Rather, it chose—properly, in my judgment—to leave reevaluation of the cost of service to the next Section 4 proceeding.[24] Panhandle has no more right to *increase* its rate of return by keeping new transportation revenues—without resorting to Section 4—than FERC has to *decrease* the rate of return using its

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[23] Panhandle's rates were last set by settlement agreement in *Panhandle Eastern Pipe Line Co.*, Docket No. RP75-102 (April 25, 1977). Until they are revised, the Commission may operate as if they were still accurate. The general rate level for Panhandle is the subject of a proceeding now under way in Docket No. RP78-62.

[24] *Cf. California Oil Co.* v. *FPC*, 315 F.2d 652, 655 (10th Cir. 1963):

> At the outset, we must recognize and emphasize that this involves the issuance of a certificate of public convenience and necessity under Section 7(e) of the Act. It is not a "rate" case under either Section 4 or Section 5 and, therefore, the complex and intricate problems as to what is a "just and reasonable" price under those sections are not before us. We have only to determine the issue of the validity of the price condition imposed upon the certificate issued to petitioner.

Section 7 powers. *See* —— F.2d at —— (pp. 12-13) *supra*. Operating on an analogy to the purchased gas adjustment procedure, the Commission decided that new transportation revenues should be credited immediately, without the delay of a Section 4 proceeding. There is nothing arbitrary or unreasonable in using this sort of interim tracking mechanism; there is, therefore, no reason to set aside the order for failure to make express findings on Panhandle's cost of service.[25]

III

Although the order requiring flow-through of new transportation revenues thus appears unobjectionable when viewed by itself, I cannot vote to affirm it in the light of the Commission's second order, which denied Panhandle's request to flow through parallel transportation costs. Admittedly, nothing in the Act or the regulations promulgated thereunder requires FERC to approve flow-through procedures for increased costs of any sort, any more than they require

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[25] Panhandle also claims that the first order is inconsistent with the decision in *Northwest Pipeline Corp.*, Docket No. RP71-154 *et al.* (March 31, 1978). In that decision Northwest Pipeline Corporation's rates were increased pursuant to a purchased gas adjustment clause. Southwest Gas Corporation intervened in the proceeding for the purpose of requesting that Northwest be required to flow through transportation revenues via the purchased gas account. FERC rejected this request, noting that treatment of transportation revenues is properly considered in the court of a § 7 or a § 4 proceeding. Obviously, that conclusion does not conflict with the decision in the first order under review here.

FERC to approve flow-through procedures for increased revenues.[26] The Commission, however, has insisted upon a flow-through of new revenues from transportation services, and therefore assumes the burden of explaining why it treats revenues differently from parallel costs. I have searched through the orders and the brief of the Commission for an adequate explanation; finding none, I conclude that both orders must be vacated and remanded to the Commission for consistent treatment.

The Commission has not suggested any technical distinctions between new transportation costs and revenues that would justify their opposite treatment. Presumably, the data on which to base the decisions are of the same sort. It would seem that new transportation costs bear the same relationship to new transportation revenues that increases in purchased gas costs bear to decreases in purchased gas costs. The Commission adopted evenhanded treatment of the purchased gas costs; it suggests no plausible reason why evenhanded treatment of new transportation costs and revenues is not desirable as well.

The Commission's sole explanation why transportation revenues, but not costs, should be credited to the purchased gas account is:

> The purpose of the [revenue crediting] condition was to assure that the pipelines' customers share

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[26] Panhandle makes no claim that FERC is required by statute or regulation to approve transportation cost flow-throughs, nor does the majority. *See* majority op., —— F.2d at —— (p. 40).

> in the revenues received from such transportation service, since the rates that the customers pay are based on costs and revenues established in the pipelines' most recent approved rate case. The nonrecurring short term transportation services enable the company to retain revenues attributable to these volumes, absent the Commission's recently imposed crediting conditions. Furthermore, including transportation costs under PGA provisions is not permitted unless the pipeline has an approved "tracking" provision in its tariff. * * * [27]

That, of course, is no explanation at all. If Panhandle's customers should receive the benefits accruing from their shares of the fixed costs, then they should also bear the costs incurred in obtaining additional benefits. When the Commission adopts a flexible approach to accounting for revenues, it may not retreat behind the lack of formal "tracking authority" when it denies parallel treatment for related costs. The Commission must indeed seek the "lowest possible reasonable rate consistent with the maintenance of adequate service in the public interest." [28] But lower rates are not always synonymous with just and reasonable rates. I have always understood the theory of ratemaking as setting rates

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[27] Findings and Order after Statutory Hearing Issuing Certificate of Public Convenience and Necessity[,] Granting Intervention, and Denying Petition at 5 (April 17, 1978), *reprinted at* JA 119.

[28] *Atlantic Refining Co.* v. *Public Service Comm'n, supra* note 9, 360 U.S. at 388.

at a level such that revenue will be equal to cost plus a reasonable profit. Any procedure that increases cost while forbidding an increase in related revenue must necessarily deviate from that ideal.

FERC argues that the ill effects of this uneven treatment will be offset by revenue from Panhandle's increased sales of the gas being transported. According to this theory, Panhandle would benefit from the increased sales because the price of each unit of new gas sold will include a portion of the fixed costs for the entire system. Since those fixed costs are already fully allocated to existing sales, the fixed cost component of the new sales would offset the transportation losses.

FERC's theory would come true, however, only if the fixed costs per unit, multiplied by the number of new units of gas sold, were equal to the total of new transportation costs.[29] There is no reason to assume this to be true: in this case it is embarrassingly false. The price Panhandle must pay the producers for the new supplies of natural gas is 102.83 cents per Mcf; the cost of transportation by others is 58.53 cents per Mcf. Panhandle's highest charge for gas is 118.22 cents per Mcf. Thus far from reaping any gains from additional fixed cost charges, Panhandle will lose 43.14 cents per Mcf on these new sales—a total of $1,576,435 per year—assuming that the com-

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[29] This assumes that the price the pipeline receives for new gas will be equal to the variable cost per unit of the new gas plus the fixed cost per unit as previously set by ratemaking. Often, however, this assumption is untrue—and the pipeline's revenue shortfall will be even more dramatic.

pany incurs *no other costs* in connection with the new sales.[30]

This manner of penalizing natural gas companies for bringing new supplies of natural gas to their customers can only harm the public. In order to provide customers with the service they require, natural gas companies have had to search far for new supplies of gas, and to procure transportation from other pipelines when those new supplies are not located along established pipeline routes. The Commission has no power to force a company to pursue new gas supplies diligently; its only inducement to a natural gas company is to permit a fair return on investment in new supplies. The consequences of FERC's orders in this case are easily predictable: the pipeline companies will be reluctant to procure distant supplies of gas, or they will file more frequent Section 4 increases, with all the problems such frequent filings entail. Neither possibility is in the consumers' interest. It is not the job of this court to dictate what incentives the Commission should offer the natural gas companies. But it is appropriate to note that orders that are arbitrary and unexplained may harm more than the company involved; they may hurt us all.[31]

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[30] Application for Rehearing of Panhandle Eastern Pipe Line Company, Docket No. CP78-43, at 6, *reprinted at* JA 132 (arithmetic error corrected).

[31] Panhandle also challenges the lack of an evidentiary hearing in the orders under review. This raises difficult questions about hearing requirements and waiver of such require-

CONCLUSION

The majority opinion leaves little alternative to the Commission but to abandon its attempt in this case to make interim adjustments to account for new transportation costs and revenues. The order refusing to allow cost flow-through has been affirmed; the order requiring revenue flow-through has been reversed. I respectfully suggest that my alternative disposition of the two orders [32]—to vacate and remand both for consistent treatment—would leave the Commission a much wider range of options to deal with this challenging problem. It might choose—as the majority apparently would require—to treat new transportation costs and revenues like any other changing factors, and await Section 3 or Section 5 proceedings before adjusting Panhandle's rates. It might choose to adopt a procedure for immediate flow-through of new transportation costs and revenues. It might choose to distinguish between short- and long-term transportation arrangements, or between companies with and without purchased gas cost ad-

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ments. Given my suggested disposition of this appeal, these questions need not be resolved: on remand FERC would presumably accord the full procedural protections mandated by the statute or provided in the sound discretion of the agency.

Panhandle also has argued that the challenged orders are discriminatory. In my view, FERC has satisfactorily explained the difference in treatment accorded in the cited instances.

[32] I join in the majority's disposition of the third order. *See* text and notes at notes 5-6 *supra*.

justment clauses. It should have wide latitude in its decision making so that it may construct necessary safeguards for the public interest. I would insist simply that the Commission choose a procedure that treats like accounts alike. Evenhandedness we should require; all other policy choices should be left to the Commission.

APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA

September Term, 1979

[Filed Dec. 20, 1979]

No. 78-1356

PANHANDLE EASTERN PIPE LINE COMPANY,
PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT

78-1630

PANHANDLE EASTERN PIPE LINE COMPANY,
PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT

78-1960

PANHANDLE EASTERN PIPE LINE COMPANY,
PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT

PETITIONS FOR REVIEW OF ORDERS OF THE
FEDERAL ENERGY REGULATORY COMMISSION

Before: WRIGHT, Chief Judge; WILKEY, Circuit Judge and LARSON *, United States Senior District Judge for the District of Minnesota

JUDGMENT

These causes came on to be heard on petitions for review of orders of the Federal Energy Regulatory Commission and were argued by counsel. On consideration of the foregoing, it is

A true copy:

Test: George A. Fisher
United States Court of Appeals
for the
District of Columbia Circuit

By: /s/ Catherine Bateman
Deputy Clerk

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* Sitting by designation pursuant to 28 U.S.C. § 292(d).

ORDERED AND ADJUDGED, by this Court, that the order in No. 78-3156 is hereby vacated and the case is remanded to the Federal Energy Regulatory Commission for further proceedings; the order in No. 78-1630 is hereby vacated in part, and affirmed in part, and the case is remanded to the Commission for further proceedings; and the order in No. 78-1960 is hereby vacated in part, and affirmed in part, and the case is remanded to the Commission for further proceedings, all in accordance with the opinion of this Court filed herein this date.

Per Curiam

For the Court:

/s/ George A. Fisher
GEORGE A. FISHER
Clerk

Dated: 20 December 1979

Opinion for the Court filed by Circuit Judge Wilkey.

Opinion concurring filed by Chief Judge Wright.

APPENDIX C

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

CERTIFICATE
(transportation)

Before Commissioners: Charles B. Curtis, Chairman;
Don S. Smith,
Georgiana Sheldon,
Matthew Holden, Jr., and
George R. Hall

Docket No. CP77-473

NORTHERN NATURAL GAS COMPANY

Docket No. CP77-479

PANHANDLE EASTERN PIPE LINE COMPANY
TRUNKLINE GAS COMPANY

Docket No. CP77-532

COLUMBIA GAS TRANSMISSION CORPORATION

Docket No. CP77-543

TRANSCONTINENTAL GAS PIPE LINE CORPORATION

FINDINGS AND ORDER AFTER STATUTORY HEARING ISSUING CERTIFICATES OF PUBLIC CONVENIENCE AND NECESSITY, GRANTING PETITIONS TO INTERVENE, AND DENYING REQUEST FOR FORMAL HEARING

(Issued December 16, 1977)

On October 1, 1977, pursuant to the provisions of the Department of Energy Organization Act (DOE Act), Public Law 95-91, 91 Stat. 565 (August 4, 1977) and Executive Order No. 12009, 42 Fed. Reg. 46267 (September 15, 1977), the Federal Power Commission ceased to exist and its functions and regulatory responsibilities were transferred to the Secretary of Energy and the Federal Energy Regulatory Commission (FERC) which, as an independent commission within the Department of Energy, was activated on October 1, 1977.

The "savings provisions" of Section 705(b) of the DOE Act provide that proceedings pending before the FPC on the date the DOE Act takes effect shall not be affected and that orders shall be issued in such proceedings as if the DOE Act had not been enacted. All such proceedings shall be continued and further actions shall be taken by the appropriate component of DOE now responsible for the function under the DOE Act and regulations promulgated thereunder. The functions which are the subject of these proceedings were specifically transferred to the FERC by Section 402(a)(1) or (2) of the DOE Act.

The joint regulation adopted on October 1, 1977, by the Secretary and the FERC entitled "Transfer of Proceedings to the Secretary of Energy and the FERC," 10 CFR ——, provided that this proceeding would be continued before the FERC. The FERC takes action in this proceeding in accordance with the above-mentioned authorities.

Northern Natural Gas Company (Northern) filed on June 29, 1977, in Docket No. CP77-473 an application, Panhandle Eastern Pipe Line Company (Panhandle) and Trunkline Gas Company (Trunkline) filed on June 30, 1977, in Docket No. CP77-479 a joint application as supplemented October 19, 1977, Columbia Gas Transmission Corporation (Columbia) filed in Docket No. CP77-532 an application on July 28, 1977, and Transcontinental Gas Pipe Line Corporation (Transco) filed in Docket No. CP77-543 an application on August 3, 1977, as supplemented August 17, 1977, with the FPC pursuant to Section 7(c) of the Natural Gas Act for certificates of public convenience and necessity authorizing the transportation in interstate commerce of up to 1,800 Mcf of natural gas per day for Libby-Owens-Ford Company (LOF) for a term of eight years, all as more fully set forth in the applications in this proceeding.

LOF has acquired gas reserves in place in the Fritzlen Field, Woods County, Oklahoma, and has entered into transportation agreements with Panhandle, Trunkline, Northern, Columbia and Transco to have such gas transported to four plants located

one each in Laurinburg, North Carolina, and Mason City, Iowa, and two near Toledo, Ohio. LOF will construct approximately eight miles of gathering line to connect three wells to Panhandle's existing system at a point near Alva, Woods County, Oklahoma; and Panhandle will deliver the gas to either Northern, Columbia or Transco. The gas to be delivered to Transco will be delivered to Trunkline by Panhandle for subsequent redelivery by Trunkline to Transco.

Pursuant to an agreement dated December 30, 1976, LOF has purchased for $4,878,499 the working interest of Damson, John T. Pickens, and Publishers Petroleum, a Division of the Oklahoma Publishing Company, aggregating 91 percent in three wells presently shut-in in Woods County. LOF states reservoir engineering reports estimate that there are approximately 7,833,500 Mcf of recoverable reserves underlying the three wells. LOF will install dehydrating and liquid separation and compression facilities and approximately eight miles of gathering pipeline. The total cost of delivering the gas to Panhandle is estimated to be $1.62 per Mcf the first year and an average cost over the next seven years of $1.73 per Mcf. These estimates include the total component cost of purchasing and producing the gas.

Data compiled from FPC Form 45 reports of intrastate gas prices received by producers in Oklahoma during the second quarter of 1977 indicate a range of 31.89 cents per Mcf to $1.9609 per Mcf with an average price of $1.6463 per Mcf. Since LOF estimates the total cost of its gas including the cost of

facilities to deliver the gas to Panhandle to be $1.62 per Mcf the first year and $1.73 for the remaining seven years of the proposed transportation arrangement, the cost of the gas is well within the range of new contract intrastate prices for Oklahoma. LOF has stated in a letter dated October 14, 1977, that the average heat content of the gas would be 1,130 Btu per cubic foot.

LOF indicates that if the subject gas is not sold for industrial use, it would be sold in the intrastate market at the highest possible prices.

Pursuant to a transportation agreement dated March 31, 1977, Panhandle agrees to provide firm deliveries for the account of LOF in the amounts of 450 Mcf per day to Transco at Cow Island, Louisiana, 300 Mcf per day to Northern at Mullinville, Kansas, 500 Mcf per day to Transwestern Pipeline Company (Transwestern) in Hansford County, Texas, and 550 Mcf per day to Columbia at Maumee, Ohio. Additionally, Panhandle and Trunkline agree to transport up to 1,200 Mcf per day on a best efforts basis which gas is to be nominated on a monthly basis by LOF for delivery to the other transporters. Transwestern has not filed for authorization to transport gas and no deliveries to Transwestern are anticipated at the present time. LOF has a plant in California which has no need for the gas at this time. If its gas supplies are curtailed in the future, LOF would attempt to have gas transported to it via Transwestern and a California distributor.

Northern, pursuant to a transportation agreement with LOF dated June 9, 1977, proposes to transport

on a best-efforts basis up to 300 Mcf of natural gas per day from Panhandle at an existing interconnection near Mullinville, Kansas, and deliver such gas to Interstate Power Company (Interstate) at the Mason City town border station, Cerro Cordo County, Iowa. LOF states in a letter dated May 31, 1977, that Interstate has agreed to transport the gas to LOF's Mason City plant.

Columbia proposes to transport up to 550 Mcf per day for LOF pursuant to a transportation agreement dated June 27, 1977, from an existing interconnection with Panhandle in Maumee, Lucas County, Ohio, to Columbia Gas of Ohio, Inc. (Columbia Ohio) for ultimate delivery to two LOF plants located near Toledo, Ohio. Columbia has agreed to transport the gas subject to the limits of its pipeline capacity and to its firm service obligations. The agreement also provides for the diversion of gas to Columbia in the event of an emergency effecting Priority 1 requirements.

Pursuant to a gas transportation agreement dated June 22, 1977, Transco proposes the transportation of up to 420 Mcf of gas per day on an interruptible basis for delivery to North Carolina Natural Gas Corporation (NCNG) for the account of LOF. LOF will deliver the subject gas to Panhandle in Oklahoma which will cause its wholly-owned subsidiary, Trunkline, to deliver an equivalent volume to Transco at Cow Island, Louisiana, or other mutually agreeable existing interconnections. There will be no additional transportation charge to LOF for volumes redelivered by Trunkline.

Panhandle proposes a firm monthly charge of $7,650 based upon a transmission system cost per 100 miles of 2.5 cents. Panhandle will retain 6.0 percent of the volumes delivered to Transco and 8.0 percent of the volumes delivered to Columbia for compressor fuel. There is no fuel usage reduction for volumes delivered to Northern due to the short distances of haul. The transportation agreement dated March 31, 1977, provides for a daily contract demand level of 1,800 Mcf per day for a term of 8 years. LOF has the option of changing the contract demand level in the fourth year. The agreement also provides that Panhandle will deliver an additional 1,200 Mcf of natural gas per day on a best efforts basis. The charge for volumes delivered in excess of the 1,800 Mcf per day firm volumes would be the unit cost at the respective point of redelivery. The agreement further specifies that should Panhandle be unable to receive volumes tendered by LOF, the charges would be reduced in accordance with reduced deliveries as follows: 15.43 cents per Mcf for Transco; 4.30 cents per Mcf for Northern; 23.10 cents per Mcf for Columbia and 8.40 cents per Mcf for Transwestern.

The firm monthly charge includes deliveries to Transwestern for the account of LOF. Transwestern has not filed for authorization to transport any gas for LOF. Until Transwestern receives appropriate authorization, Panhandle's authorization herein is conditioned upon the reduction in its monthly charge to LOF by the amount attributable to deliveries to

Transwestern. This would reduce the charge by $1,280 per month from $7,650 to $6,370.

The 2.5 cents per 100 miles of haul represents Panhandle's system transmission cost-of-service, excluding fuel. Subsequent to the transportation agreement with LOF, an order approving a settlement agreement in Panhandle's Docket No. RP75-102 was issued reducing the cost-of-service to 2.41 cents per 100 miles of haul. Panhandle states that upon authorization herein, it will file the subject agreement as a special rate schedule as a part of its FERC Gas Tariff, Original Volume No. 2, and reflect the rate of 2.41 cents per 100 miles of haul which would reduce the firm monthly charge of $7,366. The rates in Docket No. RP75-102 provide for the recovery of all justifiable costs for gas to be sold or transported but do not include the transportation of gas as proposed herein. Since Panhandle will recover its costs through normal operations, any revenues from the instant transportation service shall be credited to its unrecovered purchased gas cost account.

Northern has agreed to transport gas for LOF on a best efforts basis and will charge 23.94 cents per Mcf. It will retain 4.0 percent of such volumes transported to recover unaccounted-for gas and compressor fuel. Since all of Northern's cost will be recovered based on projected sales which do not include the transportation volumes herein, any revenues shall be credited to Northern's unrecovered purchase gas cost account.

Columbia proposes a transportation charge of 22.21 cents per Mcf for all gas transported for the account

of LOF. It will retain 3.1 percent of such volumes to recover fuel usage and unaccounted for gas.

Under a settlement approved by the Federal Power Commission in Docket No. RP75-106, beginning March 1, 1977, Columbia is obligated to credit to its deferred purchase gas account all revenues for transportation performed pursuant to Section 2.68 and/or Section 2.79 of the General Policy and Interpretations.

Transco will perform the subject transportation service for LOF at a charge of 29.8 cents per dekatherm (dt). It will retain 3.8 percent of the volumes transported for compressor fuel and unaccounted for gas.

Although the proposed term of service in the instant applications is eight years, certificates of public convenience and necessity are being issued for a two-year period without prejudice to refiling pending the outcome of the application for rehearing submitted by Natural Gas Pipeline Company of America, *et al.*, in Docket No. CP77-71, *et al.* (See also Docket No. CP77-344,temporary certificate issued July 15, 1977.) The instant authorizations herein will be conditioned consistently with the orders issued in Docket Nos. CP77-71, *et al.*, and CP77-344.

In an affidavit dated April 13, 1977, LOF states that the subject gas would be utilized for Priority 2 process uses. The Laurinburg, North Carolina, plant manufactures float glass and is the principal supplier of glass to LOF's Mason City, Iowa, Clinton, North Carolina, and Toledo, Ohio, plants. The high priority gas is used in the annealing lehr where

molten glass is gradually cooled and the tempering furnace which increases the strength of the glass. Both operations are direct fired processes which require precise temperature controls. LOF has installed propane facilities to meet short term interruptions, but states that its continued use is uneconomical. LOF anticipates 100 percent curtailment at times during the 1977-78 winter period with Transco's projecting an average curtailment of 17 percent into Priority 1 for the 1977-78 winter period.

The two plants located near Toledo, Ohio, manufacture float glass, filmed glass and glass used in the automobile industry. The gas is used in annealing lehrs and tempering furnaces. LOF has received estimated curtailment projections from its supplier for the 1977-78 winter period of 20 percent of its Priority 3 requirements and 10 percent of its Priority 2 requirements assuming normal winter weather. Although propane facilities are available on a standby basis, extended use of propane would be uneconomical in the competitive glass industry and could cause plant shutdowns.

LOF's Mason City plant produces thermopane insulating glass with GlasSeal edge. This type of glass has a sealed air space between two glass panes which is used in the construction of homes and buildings to conserve energy. The edge fusion process is performed in a glass seal furnace, which is designed specifically for natural gas and requires precise temperature control and flame characteristics of a clean burning gaseous flame. Although LOF states its Priority 2 requirements are 500 to 550 Mcf per day,

data in Northern's ongoing curtailment case in Docket Nos. RP76-52, *et al.*, indicate that LOF's Mason City plant has Priority 2(b) requirements of 350 Mcf per day. LOF states it has transferred two glass seal furnaces from its Toledo plant to consolidate all GlasSeal thermopane production in one facility. LOF's estimated requirements of 500 Mcf to 550 Mcf per day include the two additional furnaces. The natural gas utilized by the two furnaces does not constitute a new sale from Northern's supply, but does represent an increase in LOF's requirements. LOF states that its supplier, Interstate, has curtailed LOF completely and from November 1, 1976, through December 18, 1976, LOF was required to pay Interstate a surcharge for Interstate's use of propane and for its emergency gas purchases. LOF has propane standby facilities but states the extended use of propane would be uneconomical.

Northern does not project any curtailments to its Priority No. 1 and 2(b) categories for the 1977-78 winter period. However, Northern projects deliveries to its customers within existing contract demands which have remained unchanged for several years. In cases where distributors have added loads in excess of contract demands, such requirements above contract demands are being met with peak shaving facilities which appear to be the case with Interstate. Although LOF is being served its volumes classified in Priority No. 2, it is being charged for interstate's peak shaving expenses. While it does not appear that the plant would be forced to shut

down due to lack of fuel for the existing glass seal furnaces, it appears that the two additional furnaces would have to be operated entirely on propane unless the instant authorization is granted.

After due notice by publication in the Federal Register in Docket No. CP77-473 on July 19, 1977 (42 FR 37046), in Docket No. CP77-479 on July 19, 1977 (42 FR 37047), in Docket No. CP77-532 on August 17, 1977 (42 FR 41448) and in Docket No. CP77-543 on August 29, 1977 (42 FR 43450), timely petitions to intervene in Docket No. CP77-473 were filed by North Central Public Service Co., Division of Donovan Companies, Inc. (North Central), Minnesota Gas Company (Minnesota), Iowa Public Service Company (Iowa), and Interstate. A late petition to intervene in Docket No. CP77-473 was filed by Iowa Power and Light Company (Iowa Power), but no reason was given for the untimely filing. LOF filed petitions to intervene in support of these proceedings in Docket Nos. CP77-473, CP77-479, CP77-532 and CP77-543. Northern Illinois Gas Company (NI-Gas) filed petitions to intervene in Docket Nos. CP77-473 and CP77-479 requesting a formal hearing. NI-Gas states that the basis for a hearing is required to determine: (1) whether industrial customers should be allow to preempt pipeline capacity for an extended period of time; (2) whether the service contemplated by the arrangements between Northern, Panhandle, Trunkline and LOF permit existing distribution customers to make emergency purchase and transportation arrangements to offset curtailments

which take priority over LOF's contract demand; (3) whether LOF should be required to sell a portion of its gas to the pipeline companies for resale; and (4) whether the transportation charges are compensatory and the volumes of fuel usage gas retained by the pipeline companies are sufficient.

The issues which are set forth by NI-Gas as requiring a formal hearing on the applications can and are resolved herein, based on the existing record, by appropriately conditioning the authorizations or have heretofore been resolved. There are not issues of fact to be resolved. A formal hearing would serve no useful purpose. The proposed transportation charge by Northern reflects recent system transmission cost-of-service as set forth in Northern's pending rate proceeding in Docket No. RP77-5*, and the fuel usage volumes to be retained are derived from operating experience. The transportation charged by Panhandle reflects recent transmission cost-of-service allowed in Docket No. RP75-102, and the fuel usage volumes to be retained are derived from operating experience. Moreover, the revenues from the subject services will be required to be credited to Northern's and Panhandle's unrecovered purchased gas cost accounts, thus inuring to the benefit of all of their resale customers. Requiring LOF to sell a portion of its gas to Northern and Panhandle would have an insignificant effect on their overall systems and for at least part of the year would go to end users in lower priorities; however, any diversion of the gas from LOF would be of major significance to LOF.

The volumes proposed to be transported by Northern on a best-efforts basis would be subordinate to volumes of gas being delivered to existing firm customers; and although the proposed service by Panhandle and Trunkline is described as firm transportation, a condition hereinafter imposed subordinating said service to the pipeline companies' existing firm requirement will preclude a preemption of pipeline capacity. With regard to the effect of the proposed service upon emergency purchase and transportation arrangements by distribution customers, the condition subordinating the service authorized herein will also preclude LOF from receiving any service when firm deliveries by the pipeline companies are being jeopardized. Furthermore, LOF will receive no more gas than it is entitled to from its own distributor suppliers so that no preemption of capacity or service will occur. In addition, LOF's gas will be delivered to Northern at a point on its mainline transmission system which consists of four large diameter pipelines with looped portions and an additional 300 Mcf per day would be an insignificant volume of gas. NI-Gas' requests for formal hearings will not be granted.

A notice of intervention was filed in Docket No. CP77-473 by Metropolitan Utilities District of Omaha. No further peitions to intervene, protests to the granting of the applications, or further notices of intervention have been filed.

At a hearing held on December 7, 1977, the Commission on its own motion received and made a part of the record in these dockets all evidence, including the applications, affidavits, and exhibits thereto, sub-

mitted in support of the authorizations sought herein, and upon consideration of the record,

The Commission finds:

(1) Applicant, Northern Natural Gas Company, a Delaware corporation having its principal place of business in Omaha, Nebraska, is a "natural-gas company" within the meaning of the Natural Gas Act, as heretofore found by order issued April 6, 1943, in Docket No. G-280 (3 FPC 967).

(2) Applicant, Panhandle Eastern Pipe Line Company a Delaware corporation having its principal places of business in Houston, Texas, and Kansas City, Missouri, is a "natural-gas company" within the meaning of the Natural Gas Act, as heretofore found by order issued September 23, 1942, in Docket Nos. G-200 and G-207 (3 FPC 273).

(3) Applicant, Trunkline Gas Company, a Delaware corporation having its principal places of business in Houston, Texas, and Kansas City, Missouri, is a "natural-gas company" within the meaning of the Natural Gas Act, as heretofore found by order issued April 29, 1949, in Docket No. G-882 (8 FPC 250).

(4) Applicant, Columbia Gas Transmission Corporation, a Delaware corporation having its principal place of business in Charleston, West Virginia, is a "natural-gas company" within the meaning of the Natural Gas Act, as heretofore found by order issued March 10, 1971, in Docket No. CP71-132 (45 FPC 398).

(5) Applicant Transcontinental Gas Pipe Line Corporation, a Delaware corporation having its principal place of business in Houston, Texas, is a "natural-gas company" within the meaning of the Natural Gas Act, as heretofore found by order issued November 18, 1948, in Docket No. G-1143 (7 FPC 145).

(6) The services hereinbefore described as more fully described in the applications in Docket Nos. CP77-473, CP77-479, CP77-532 and CP77-543 involve the transportation of natural gas in interstate commerce, subject to the jurisdiction of the Commission, and said services are subject to the requirements of Subsections (c) and (e) of Section 7 of the Natural Gas Act.

(7) Applicants are able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Natural Gas Act and the requirements, rules, and regulations of the Commission thereunder.

(8) The transportation of natural gas by Applicants is required by the public convenience and necessity and certificates therefor should be issued as hereinafter ordered and conditioned.

(9) The issues raised by NI-Gas in its petitions to intervene filed in Docket Nos. CP77-473 and CP77-479 do not require a formal hearing for resolution.

(10) Inasmuch as Iowa Power is a customer of Northern and acceptance of its late petition to intervene in Docket No. CP77-473 will not cause delay in

said proceeding, good cause exists for permitting the late filing.

(11) Participation by the petitioners to intervene in the proceedings in which they have filed may be in the public interest.

The Commission orders:

(A) A certificate of public convenience and necessity is issued authorizing Northern to transport up to 300 Mcf of natural gas per day on a best-efforts basis in interstate commerce for a period of two years, as hereinbefore described and as more fully described in the application filed in Docket No. CP77-473, upon the terms and conditions of this order.

(B) A certificate of public convenience and necessity is issued authorizing Panhandle and Trunkline to transport up to 1,800 Mcf of natural gas per day on a firm basis and up to 1,200 Mcf of natural gas per day on a best-efforts basis in interstate commerce for a period of two years, as hereinbefore described and as more fully described in the application filed in Docket No. CP77-479, upon the terms and conditions of this order.

(C) A certificate of public convenience and necessity is issued authorizing Columbia to transport up to 550 Mcf of natural gas per day on a best efforts basis in interstate commerce for a period of two years, as hereinbefore described and as more fully described in the application filed in Docket No. CP77-532, upon the terms and conditions of this order.

(D) A certificate of public convenience and necessity is issued authorizing Transco to transport up to 450 Mcf of natural gas per day on a best efforts basis in interstate commerce for a period of two years, as hereinbefore described and as more fully described in the application filed in Docket No. CP77-543, upon the terms and conditions of this order.

(E) The certificates issued by paragraphs (A), (B), (C) and (D) above and the rights granted thereunder are conditioned upon Applicants' compliance with all applicable Commission Regulations under the Natural Gas Act and particularly the general terms and conditions set forth in paragraphs (a) and (e) of Section 157.20 and in Part 154 of such Regulations.

(F) The certificates issued by paragraphs (A), (B), (C) and (D) above and the rights grantsd thereunder are conditioned further as follows:

(1) The volumes of gas transported shall be utilized only for Priority 2 uses and Priority 3 uses which would be Priority 2, but for an interruptible contract as defined in Section 2.78 of the Commission's General Policy and Interpretations (18 CFR 2.78). In no event shall the total volumes delivered to LOF exceed its contract demands with its suppliers.

(2) LOF shall reduce the volumes it would receive under the curtailment plan of its existing natural gas suppliers for Priority 2 and Priority 3 uses as defined above to the extent that the volumes of gas transported

under the transportation certificates exceed the volumes of curtailment experienced by LOF in the eligible Priority 2 and Priority 3 categories. However, for purposes of this condition, the transportation volumes for LOF's Mason City plant shall be in addition to the existing Priority 2 uses up to a maximum of 550 Mcf per day.

(3) Applicants shall each submit a monthly report consisting of an original and four copies to the Commission indicating the name of the producer, the point of delivery from the producer, the volumes received and transported, the volumes delivered, the point of delivery to the distributors and the name of the distributors. Such reports shall be filed under oath within 20 days after the end of each month included in the term of the transportation certificates. The pipelines shall file reports for any month during which gas was not transported. In addition, the first monthly reports shall also state the date of initial delivery.

(4) LOF shall provide Applicants with a monthly report which shall be transmitted to the Commission as an attachment to the reports required by (3) above. Such report shall contain the amount of natural gas consumed at the plants during the month covered by the report, the end use of such consumption according to the end-use priorities contained in 18 CFR 2.78, the amount of natural gas consumed from other sources during the month, a list of such other

sources and the end use of the gas from such sources.

(5) Panhandle's proposed firm monthly charge to LOF shall be reduced by the proposed charge to deliver gas to Transwestern until such time as Transwestern receives appropriate authorization to transport gas for the account of LOF. Further, revenues from the instant transportation service shall be credited to Panhandle's unrecovered purchased gas account.

(6) Panhandle shall file tariff sheets reflecting transportation rates based on its cost of service as approved by order issued April 25, 1977, in Docket No. RP75-102.

(7) The volumes of gas transported for LOF by Northern, Panhandle and Trunkline shall be subordinate to existing firm services to their other customers.

(8) The proposed transportation rate by Columbia shall be adjusted to reflect the final outcome of proceedings in Docket No. RP76-95. Further, the revenues from such transportation service shall be credited to Columbia's unrecovered purchased gas account.

(9) Transco's proposed transportation rate shall be subject to the final determination in Docket Nos. RP76-136 and RP77-26.

(10) Northern's proposed transportation rate shall be subject to the final determination in Docket No. RP77-56. In addition, the reve-

nues resulting from such transportation service shall be credited to Northern's unrecovered purchased gas account.

(G) NI-Gas' requests for formal hearing in Docket Nos. CP77-473 and CP77-479 are denied.

(H) The petitioners to intervene are permitted to intervene in the proceedings in which they filed subject to the rules and regulations of the Commission: *Provided, however,* that participation of such intervenors shall be limited to matters affecting asserted rights and interests as specifically set forth in their petitions to intervene; and *Provided, further,* that the admission of such interveners shall not be construed as recognition by the Commission that they might be aggrieved because of any order of the Commission entered in these proceedings.

By the Commission.

[SEAL]

KENNETH F. PLUMB,
Secretary.

APPENDIX D

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY
COMMISSION

REHEARING

Before Commissioners: Charles B. Curtis, Chairman;
Don S. Smith,
Georgiana Sheldon,
Matthew Holden, Jr.,
and George R. Hall

Docket No. CP77-479

PANHANDLE EASTERN PIPE LINE COMPANY

ORDER ON REHEARING AMENDING ORDER ISSUING CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY

(Issued February 22, 1978)

On January 13, 1978, Panhandle Eastern Pipe Line Company (Panhandle) filed an application for rehearing of the Commission's order issued December 16, 1977, in Docket No. CP77-479 granting a certificate of public convenience and necessity pursuant to Section 7(c) of the Natural Gas Act authorizing the transportation of natural gas from Woods County, Oklahoma, for the account of Libby-Owens-Ford Company (LOF). Four pipelines will provide portions of the transportation service for order issued February 10, 1978, the Commission LOF, with Panhandle as the initial transporter. By granted rehearing for further consideration.

In its application for rehearing, Panhandle asserts the Commission erred in requiring Panhandle to credit all revenues from the instant transportation service to its unrecovered purchased gas account. Panhandle requests reconsideration of the above condition for the following reasons:

(1) The condition ignores any costs which may be incurred in performing the transportation service;

(2) The transportation revenues are required to be credited to the purchased gas cost account, but there is no relationship between purchased gas costs and transportation revenues;

(3) There is no assurance that purchased gas adjustment tracking will be permitted throughout the eight-year period for which transportation authorization was requested;

(4) The imposition of such a provision against Panhandle without a similar provision for another of the transporters, Transcontinental Gas Pipeline Corporation (Transco) is discriminatory; and

(5) There is no provision permitting Panhandle to recover automatically its increased transportation costs.

Since the transportation service is made possible by the existence of unused capacity on Panhandle's system and the costs associated with that capacity are borne by Panhandle's resale gas customers, the revenues from such service should benefit the pipeline customers which have paid for unused capacity.

Crediting of such revenues to Panhandle's unrecovered purchased gas cost account ensures that Panhandle's resale gas customers will be the beneficiaries of the transportation revenues.

With regard to Panhandle's objection that there is no assurance the purchased gas adjustment tracking will be permitted throughout the proposed eight-year transportation term, the order issued in the instant proceeding limits Panhandle's transportation service to two years without prejudice to refiling for an extension of time. Therefore, we need not consider the assurance of a tracking provision beyond the two-year period at this time.

Panhandle alleges that the crediting provision applied to it is discriminatory because such a provision is not applied to Transco. Transco has previously agreed to credit transportation revenues to its unrecovered purchased gas cost account and the treatment of such revenues is an issue in Transco's rate proceedings in Docket Nos. RP76-136 and RP77-26 and in Docket No. RP77-108.

In view of Panhandle's allegations in its application for rehearing that it will incur actual incremental costs for the proposed transportation service, it appears reasonable to permit Panhandle to recover the demonstrated actual jurisdictional out-of-pocket costs. In order that the remainder of such transportation revenues redound to the benefit of all of Panhandle's resale gas customers, a portion of such revenues attributable to Panhandle's jurisdictional customers should be credited to Panhandle's unre-

covered purchased gas cost account. The revenues to be credited to Account 191 of the Uniform System of Accounts for Natural Gas Companies for the benefit of jurisdictional resale gas customers should be determined each month by multiplying the total transportation revenues received from LOF, less out-of-pocket costs, for the month by the ratio of jurisdictional sales volumes to total sales volumes for the month. In the event Panhandle's other transportation costs are preventing it from earning a reasonable return, it is free at any time to submit a general rate change under Section 4(e) of the Natural Gas Act.

Accordingly, in view of the above, the Commission's order issued December 16, 1977, in Docket No. CP77-479, will be amended so as to require the crediting of the jurisdictional portion of any excess revenues generated over and above the out-of-pocket costs incurred in performing the subject transportation service to Panhandle's Account 191.

The Commission finds:

Based upon information supplied in the application for rehearing, it is necessary and appropriate in carrying out the provisions of the Natural Gas Act to grant said application in part; and the public convenience and necessity require that the order issuing a certificate of public convenience and necessity be amended accordingly.

The Commission orders:

(A) Panhandle's application for rehearing is granted as set forth below and in all other respects is denied.

(B) The Commission's order issued December 16, 1977, in Docket No. CP77-479, is amended so as to authorize the crediting of any excess revenues generated over and above the demonstrated actual out-of-pocket costs incurred in performing the subject transportation service attributable to jurisdictional business to Panhandle's Account 191 of the Uniform System of Accounts for Natural Gas Companies. Panhandle shall determine the revenues to be credited to Account 191 each month by multiplying the total transportation revenues received from LOF for the month, less out of pocket costs, by the ratio of jurisdictional sales volumes to total sales volumes for the month.

By the Commission.

[SEAL]

KENNETH F. PLUMB,
Secretary.

APPENDIX E

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY
COMMISSION

CERTIFICATE
(Transportation)

Before Commissioners: Don S. Smith,
Acting Chairman;
Georgiana Sheldon,
Matthew Holden, Jr.,
and George R. Hall

Docket No. CP78-43

TRUNKLINE GAS COMPANY

FINDINGS AND ORDER AFTER STATUTORY HEARING ISSUING CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY GRANTING INTERVENTION, AND DENYING PETITION

(Issued April 17, 1978)

On October 1, 1977, pursuant to the provisions of the Department of Energy Organization Act (DoE Act), Public Law 95-91, 91 Stat. 565 (August 4, 1977) and Executive Order No. 12009, 42 Fed. Reg. 46267 (September 15, 1977), the Federal Power Commission ceased to exist and its functions and regulatory responsibilities were transferred to the Secretary and the Federal Energy Regulatory Commission (FERC) which, as an independent commission within the Department of Energy, was activated on October 1, 1977.

The "savings provisions" of Section 705(b) of the DoE Act provide that proceedings pending before the FPC on the date the DoE Act takes effect shall not be affected and that orders shall be issued in such proceedings as if the DoE Act had not been enacted. All such proceedings shall be continued and further actions shall be taken by the appropriate component of DoE now responsible for the function under the DoE Act and regulations promulgated thereunder. The functions which are the subject of these proceedings were specifically transferred to the FERC by Section 402(a)(1) of the DoE Act.

The joint regulation adopted on October 1, 1977, by the Secretary and the FERC entitled "Transfer of Proceedings to the Secretary of Energy and the FERC," 10 CFR ——, provided that this proceeding would be continued before the FERC. The FERC takes action in this proceeding in accordance with the above mentioned authorities.

On October 25, 1977, Trunkline Gas Company, (Trunkline) filed in Docket No. CP78-43 an application proposing to transport up to 10,000 Mcf per day available to Panhandle Eastern Pipe Line Company (Panhandle) from Eugene Island (EI) Area Blocks 377 and 380, Offshore Louisiana which Panhandle will purchase from its affiliate, Pan Eastern Exploration Company (Pan Eastern).

Trunkline has an existing arrangement with Tarpon Transmission Company (Tarpon) for the transportation of gas for Trunkline from EI 377 and 380 which was authorized in Docket No. CP77-315. Tarpon will receive Panhandle's share of EI 377 and

380 gas at the producer's platform in EI 380 for delivery to Trunkline at Trunkline's existing platform located in Ship Shoal Block 274, Offshore Louisiana for further transportation by Trunkline to an existing authorized point of delivery to Panhandle near Tuscola, Illinois. The transportation service will be performed under a July 11, 1977, agreement which provides for a primary term of 10 years.

The monthly charge to Panhandle for the service will be a composite rate comprised of rates applicable to the movement of the gas through Tarpon's and Trunkline's systems. For utilization of Trunkline's capacity in Tarpon's facilities, Trunkline will charge Panhandle the unit rate paid by Trunkline to Tarpon authorized in Docket No. CP77-315 [1] subject to adjustments as provided in the Trunkline-Tarpon Transportation Contract including a minimum bill provision based upon the minimum daily obligation applicable to Pan Eastern's interest. In addition, Panhandle will reimburse Trunkline for its proportionate share of the costs of the measurement and related facilities on the producer's platform, including associated operating and maintenance expenses.

For moving the gas received in Ship Shoal Block 274 from Tarpon for Panhandle's account to Tuscola, Illinois, Trunkline will charge Panhandle $81,800 per month. Such charge is based on a contract demand quantity of 10,000 Mcf per day and the average unit cost of 26.89¢ for moving gas through

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[1] Tarpon has filed a related rate schedule to cover such service, which reflects a transportation rate of 26.26¢ per Mcf.

Trunkline's system from the point of receipt from Tarpon to the redelivery point to Panhandle at Tuscola, Illinois. The 26.89¢ per Mcf rate is based in part on Trunkline's system wide unit cost of transmission of 2.6¢ per Mcf per 100 miles of haul multiplied by the transportation mileage of 872.5 miles which yields at unit cost of 22.69¢. The remaining 4.2¢ per Mcf results from the rate Trunkline pays Tennessee for the movement of offshore gas which is brought ashore through Trunkline's South Timbalier, Offshore system from a point in Centerville, Louisiana for delivery to Trunkline at Kinder, Louisiana under Tennessee's Rate Schedule T-11.[2] Should Trunkline fail to take the contract quantity or take in excess of the contract quantity the monthly charge will be adjusted upward or downward by 26.89¢ per Mcf, as appropriate. The monthly charge is further subject to adjustment to reflect any increase or decrease resulting from any Trunkline rate proceeding or any changes in rates paid by Trunkline for transportation services provided by others.

In addition to the charge for the service, Trunkline will retain a portion of the transported volumes for fuel usage amounting to a variable percentage based on the total through put in Trunkline's Timbalier offshore system and an additional 4 percent for main line fuel usage.

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[2] Tennessee is authorized in Docket No. CP68-245 to transport up to 500,000 Mcf per day for Trunkline. Trunkline will utilize a portion of this capacity for the transportation of Panhandle's gas.

Trunkline has recently filed a rate decrease in Docket No. RP77-11. Therefore, the certificate issued herein will be conditioned to require that the rate charged by Trunkline will be collected subject to adjustment and refund depending on the determination of an appropriate rate and the appropriate disposition of the transportation revenues in Docket No. RP78-11.

Panhandle Eastern Pipe Line Company (Panhandle) filed a late petition requesting (a) permission to intervene in the subject proceeding and (b) that the Commission in granting a certificate to Trunkline Gas Company (Trunkline) provide that the transportation costs to be incurred by Panhandle be recognized and included as cost of purchased gas to Panhandle. Panhandle requests permission to include Trunkline's monthly charges with its cost of purchased gas and thus recover the costs through its PGA filings under its tariff provisions. Trunkline is a pipeline supplier of Panhandle for the purposes of the PGA sections of Panhandle's tariff.

In support of such request, Panhandle states that this treatment of incurred transportation cost is a necessary corallary to the Commission's policy applied to Panhandle in several recent cases,[3] whereby revenues received by Panhandle from transportation services performed for others be credited to Panhandle's purchased gas account. Panhandle states that in-

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[3] Docket Nos. CP77-224 (order issued February 24, 1978), CP77-479 (order issued December 16, 1977, and February 22, 1978) and CP77-653 (order issued February 22, 1978).

cluding Trunkline's transportation costs in Panhandle's cost of purchased gas account ensures that Panhandle's resale gas customers pay their fair share of the costs in the same manner as they will be the beneficiaries of the crediting of transportation revenues; thus maintaining a quid pro quo situation until the filing of a general rate change.

Panhandle argues that absent permission in the Trunkline certificate to credit charges paid Trunkline, Panhandle would be incurring transportation costs for gas purchased for its resale customers without any recognition of such increased costs since it would be crediting cost of purchased gas with revenues received from transportation service performed for others. Panhandle claims that this requirement is both inequitable and impractical.[4]

Panhandle's request that Trunkline's certificate be conditioned to permit Panhandle to credit any charges paid to Trunkline for the proposed transportation service to Panhandle's purchased gas account should be denied. The issue of Panhandle crediting transportation charges to its purchased gas account should be addressed in an appropriate Panhandle rate proceeding.

Panhandle's reliance on the Commission's recent actions in Docket Nos. CP77-224, *et al.* requiring Panhandle to credit revenues from transportation

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[4] By order of March 20, 1978, in Docket No. CP77-653, Panhandle was given the opportunity on reconsideration to present its method to resolve crediting of short-term transportation revenues

service for others to its purchased gas account as a basis for permitting the crediting of charges paid Trunkline for the proposed transportation service to its purchased gas account is misplaced. Each of the cases cited by Panhandle involves the treatment of transportation revenues under short term arrangements (two years or less). We have recently imposed conditions pertaining to disposition of revenues derived from such short terms transportation arrangements in authorizing pipelines to perform such service. The purpose of the condition was to assure that the pipelines' customers share in the revenues received from such transportation service, since the rates that the customers pay are based on costs and revenues established in the pipelines' most recent approved rate case. The nonrecurring short term transportation services enable the company to retain revenues attributable to these volumes, absent the Commission's recently imposed crediting conditions. Furthermore, including transportation costs under PGA provisions is not permitted unless the pipeline has an approved "tracking" provision in its tariff. Panhandle does not have such a provision.

Revenues and costs associated with long term transportation services (as is the case in Docket No. CP78-43, a 10 year term) should continue to be addressed in the individual pipeline company rate cases. Therefore, if the cost to Panhandle for the transportation service performed by Trunkline precludes earning a reasonable return, Panhandle should consider submitting a general rate change filing under Sec-

tion 4(e) of the Act. Panhandle is not necessarily adversely affected by their inability to automatically recover the transportation costs because each Mcf of sales includes fixed costs. To sales in excess of the level used for billing determinate purposes in its rates the additional fixed cost recovery offsets the transportation costs.

Approval of this proposed project would not constitute a major Federal action significantly affecting the quality of human environment.

After due notice by publication in the Federal Register, no protests or petitions to intervene in opposition have been filed.

On October 31, 1977, Trunkline filed tariff sheets to its FERC Gas Tariff, Original Volume No. 2 to reflect the service proposed in Docket No. CP78-43. The sheets have been designated as follows: First Revised Sheet No. 1-D, and Original Sheet Nos. 1293 through 1326, consisting of Rate Schedule T-31.

At a hearing held on April 12, 1978, the Commission on its own motion received and made a part of the record in this proceeding all evidence, including the applications and exhibits thereto, submitted in support of the authorizations sought herein, and upon consideration of the record,

The Commission finds:

(1) Trunkline Gas Company is a "natural-gas company" within the meaning of the Natural Gas Act.

(2) The transportation of natural gas hereinbefore described as more fully described in the application in this proceeding, is made in interstate commerce, subject to the jurisdiction of the Commission, and is subject to the requirements of subsections (c) and (e) of Section 7 of the Natural Gas Act.

(3) Trunkline is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Natural Gas Act and the requirements, rules and regulations of the Commission thereunder.

(5) Good cause has been shown for waiver of the notice requirements of Part 154 of the Commission's Regulations.

The Commission orders:

(A) A certificate of public convenience and necessity is issued to Trunkline Gas Company in Docket No. CP77-43 to transport up to 10,000 Mcf per day available to Panhandle from Eugene Island Area Blocks 377 and 380, Offshore Louisiana which Panhandle will purchase from its affiliate, Pan Eastern Exploration Company subject to compliance with Section 157.20(a), (c)(3), and (e) of the Regulations. Service shall commence within 60 days of the date of issuance of certificate authorization (Section 157.20 (b) of the Regulations.

(B) The rate charged by Trunkline will be collected effective subject to refund pending determination of an appropriate rate and the appropriate disposition of the transportation revenues in Docket No. RP78-11.

(C) The notice requirement of Part 154 of the Commission's Regulations are waived, and Trunkline's proposed Tariff Sheets Nos. 1293 through 1326 and First Revised Sheet No. 1-D to its FERC Gas Tariff, Original Volume No. 2 are accepted for filing to become effective on the date of this order.

(D) Panhandle's request for permission to include Trunkline's monthly transportation charges with its cost of purchased gas and to recover such costs through its PGA filings is denied.

(E) Panhandle is permitted to intervene in Docket No. CP78-43 subject to the rules and regulations of the Commission; *Provided, however,* that the participation of such intervenor shall be limited to matters affecting asserted rights and interests as specifically set forth in its petition to intervene; and *Provided, further,* that the admission of said intervenor shall not be construed as recognition by the Commission that it might be aggrieved because of any order of the Commission entered in this docket.

By the Commission.

[SEAL]

LOIS D. CASHELL,
Acting Secretary.

APPENDIX F

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY
COMMISSION

CERTIFICATE (Transportation)
REHEARING (Denied)

Before Commissioners: Charles B. Curtis, Chairman;
Don S. Smith,
Georgiana Sheldon,
Matthew Holden, Jr.,
and George R. Hall

Docket No. CP78-43

TRUNKLINE GAS COMPANY

ORDER DENYING
APPLICATION FOR REHEARING

(Issued September 25, 1978)

On April 17, 1978, we authorized Trunkline Gas Company (Trunkline), in cooperation with Tarpon Transmission Company and Tennessee Gas Pipeline Company, to transport up to 10,000 Mcf of gas per day from Eugene Island Area Blocks 377 and 380, Offshore Louisiana, to a point near Tuscola, Illinois, for Panhandle Eastern Pipe Line Company (Panhandle) to enable Panhandle to purchase gas from its affiliate, Pan Eastern Exploration Company. Our order denied Panhandle's request to include Trunkline's monthly transportation charges with its cost of

purchased gas and to recover such costs through its PGA filings. On May 16, 1978, Panhandle filed an application for rehearing of our order, objecting to this denial. On June 14, 1978, we granted the application for rehearing solely for purposes of further consideration.

We believe our denial was proper. Transporting natural gas to its customers is central to Panhandle's jurisdictional business. Its compensation for this service, whether performed with its own facilities or by employment of the services of another pipeline company, should be recovered in its rates to its customers. If such rates are inadequate, it should file for a rate increase pursuant to Section 4 of the Natural Gas Act. But we shall not permit Panhandle to include in Account No. 191, *Unrecovered purchased gas costs*, the costs incurred by it as a result of Trunkline's transportation of its gas. Such a course of action might have the effect of allowing Panhandle a rate increase when its rates, in the context of its *overall* cost of service *vis a vis* its *overall* revenues, might be fully adequate without such increase. On the other hand, these matters would be fully considered and taken into account in a Section 4 general rate proceeding.

It is true that the Commission has provided for tracking rate increases in the case of purchased gas costs in Order No. 452, 47 FPC 1049 (1972), as amended,[1] for reasons set forth therein, but this did

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[1] The ordering portions of Order No. 452, as amended, are codified at 18 CFR 154.38(d)(4).

not extend to other cost elements, including transportation costs, such as are here sought by Panhandle.

Panhandle protests denial of its requested rate treatment on the ground that in other cases, we have required pipeline companies to flow through to their jurisdictional customers the jurisdictional portion of revenues they have received for transporting gas for other pipeline companies, less out-of-pocket or incremental expenses. It maintains that this circumstance, on the basic of logic and fairness, compels the rate treatment it seeks, standing as it does in the shoes of the purchaser of such transportation. We see nothing improper in requiring this flow through of the jurisdictional portion of transportation revenues when necessary to prevent a pipeline from being unjustly enriched at the expense of customers. Since such portion is earned with facilities and resources supported by jurisdictional consumers, jurisdictional consumers are entitled to a credit therefore against purchased gas costs, as described above. In any event, any quarrel Panhandle may have with the Commission's treatment of revenues attributable to transportation services in other proceedings should be pursued in such other proceedings and not attacked collaterly in this proceeding, where they are of peripheral interest only. Such crediting is not inconsistent with denying a pipeline purchaser who receives a transportation service a rate increase based solely thereon, as in the instant case. Any such rate increase should be sought under Section 4 of the Natural Gas Act. Absent a review of a pipe-

line's overall cost of service, it would not be appropriate to authorize a rate increase in these circumstances.

Panhandle cites *Northwest Pipeline Corporation*, Docket No. RP72-154, *et al.*, order of March 31, 1978, as being inconsistent with our order in this proceeding. We do not agree. There the Commissionn had under consideration, *inter alia*, a rate increase based on various purchase gas adjustment costs. An intervenor requested that Northwest's PGA rate increase be reduced by crediting its transportation revenues to Account No. 191. The Commission denied such request as being more appropriate in a certificate proceeding involving the revenues or a general rate proceeding of Northwest. Since no such cases were pending, the Commission made its denial without prejudice to the intervenor's right to request institution by the Commission of an investigation into the overall justness and reasonableness of Northwest's jurisdictional rates pursuant to Section 5 of the Natural Gas Act. The *Northwest* case involved crediting of transportation revenues, not the pass through of charges, as in the case at bar. Besides, it was decided on procedural, rather than substantive grounds. It is clearly no precedent for the case before us.

Panhandle further cites in support of its position orders in *Tennessee Gas Pipeline Company, et al.*, Docket No. CP77-419, *et al.*, issued November 10, 1977; and *Texas Eastern Transmission Corporation, et al.*, Docket No. CP77-313, *et al.*, issued January

27, 1978, wherein the Commission permitted Tennessee and Texas Eastern to purchase storage capacity from consolidated Gas Supply Corporation and to track any approved changes in the purchase price of such storage in their rates to their customers purchasing such storage capacity. It was made clear in the *Tennessee* order that the tracking was based on the unique facts of that particular case and was not to represent a change in the Commission's general policy with respect to tracking, as set forth in Section 154.38(d)(3). The Commission further stated that the order "should not be regarded as precedent for tracking in any future *storage arrangement* involving the same or different parties." (Emphasis supplied.) The *Texas Eastern* case also involved storage arrangements. We decline to extend these exceptions relating to storage operations to general transportation situations such as the one involved in this case.

Panhandle also cites *Richmond Power & Light* v. *FERC*, No. 75-2143, CADC, decided March 13, 1978, and states that there "the Commission did not require downstream utilities to absorb the transmission costs as it seeks to do in the case of Panhandle." The *Richmond* case upheld the Commission's order in *New England Power Pool Participants, et al.*, Docket Nos. RM74-22 and E-8589, *et al.*, issued August 26, 1974, involving the "coal by wire" program, a voluntary arrangement whereby electric utilities in various parts of the country fueled mainly by coal transmitted short term energy to power pools on the east-

ern Seaboard during January-May 1974 in order to forestall imminent threats to the reliability of service as a consequence of the Arab oil embargo. This was done pursuant to a Commission policy expressed in Order No. 496, 50 FPC 1691 (1973). We do not see the *Richmond* case as possessing any precedential value in the instant proceeding because (1) it was a *negotiated settlement,* wherein consumers received concrete benefits, such as extra energy supplies during the embargo and refunds which the Commission would not otherwise have ordered and (2) it involved a coordinated response by many utilities to a special emergency situation at the behest of a stated Commission policy. Neither of these special factual situations exist in the instant proceeding.

Finally, Panhandle states that it "can show that it is not recovering its cost of service and adequate return and hereby requests a hearing to permit that showing." Panhandle is free in these circumstances to file a rate increase pursuant to Section 4 of the Natural Gas Act at any time.

The Commission finds:

Panhandle's application for rehearing presents no new facts or principles of law which warrant any modification of our April 17, 1978 order.

The Commission orders:

Panhandle Eastern Pipe Line Company's application for rehearing, filed herein May 16, 1978, is denied.

By the Commission.

[SEAL]

KENNETH F. PLUMB,
Secretary.

APPENDIX G

Section 4 of the Natural Gas Act, 15 U.S.C. 717c, provides:

> (a) All rates and charges made, demanded, or received by any nature-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.
>
> (b) No natural-gas company shall, with respect to any transportation or sale or natural gas subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.
>
> (c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this act takes effect) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all con-

tracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by any order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, State commission, or gas distributing company, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule

and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

Section 5 of the Natural Gas Act, 15 U.S.C. 717d, provides:

> (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however,* That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural-gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural-gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.
>
> (b) The Commission upon its own motion, or upon the request of any State commission, whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transportation of natural gas by a natural-gas company in cases where the Commis-

sion has no authority to establish a rate governing the transportation or sale of such natural gas.

Section 7 of the Natural Gas Act, 15 U.S.C. (Supp. II) 717f, provides in pertinent part:

> (c) (1) (A) No natural-gas company or person which will be a natural-gas company upon completion of any proposed construction or extension shall engage in the transportation or sale of natural gas, subject to the jurisdiction of the Commission, or undertake the construction or extension of any facilities therefor, or acquire or operate any such facilities or extensions thereof, unless there is in force with respect to such natural-gas company a certificate of public convenience and necessity issued by the Commission authorizing such acts or operations: *Provided, however*, That if any such natural-gas company or predecessor in interest was bona fide engaged in transportation or sale of natural gas, subject to the jurisdiction of the Commission, on the effective date of this amendatory Act, over the route or routes or within the area for which application is made and has so operated since that time, the Commission shall issue such certificate without requiring further proof that public convenience and necessity will be served by such operation, and without further proceedings, if application for such certificate is made to the Commission within ninety days after the effective date of this amendatory Act. Pending the determination of any such application, the continuance of such operation shall be lawful.

(B) In all other cases the Commission shall set the matter for hearing and shall give such reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission; and the application shall be decided in accordance with the procedure provided in subsection (e) of this section and such certificate shall be issued or denied accordingly: *Provided, however,* That the Commission may issue a temporary certificate in cases of emergency, to assure maintenance of adequate service or to serve particular customers, without notice or hearing, pending the determination of an application for a certificate, and may by regulation exempt from the requirements of this section temporary acts or operations for which the issuance of a certificate will not be required in the public interest.

(2) The Commission may issue a certificate of public convenience and necessity to a natural-gas company for the transportation in interstate commerce of natural gas used by any person for one or more high-priority uses, as defined, by rule, by the Commission, in the case of—

(A) natural gas sold by the producer to such person; and

(B) natural gas produced by such person.

* * * * *

(e) Except in the cases governed by the provisos contained in subsection (c)(1) of this section, a certificate shall be issued to any qualified applicant therefor, authorizing the whole or any part of the operation, sale, service, construc-

tion, extension, or acquisition covered by the application, if it is found that the applicant is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Act and the requirements, rules, and regulations of the Commission thereunder, and that the proposed service, sale, operation, construction, extension, or acquisition, to the extent authorized by the certificate, is or will be required by the present or future public convenience and necessity; otherwise such application shall be denied. The Commission shall have the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require.

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